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IMPACT OF CANADIAN ENERGY AND INVESTMENT POLICIES ON U.S. COMMERCE

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REPORT

together with

DISSENTING VIEWS
BY THE

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON ENERGY AND COMMERCE

U.S. HOUSE OF REPRESENTATIVES

OCTOBER 1982

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HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C., October 6, 1982.

To: MEMBERS, COMMITTEE ON ENERGY AND COMMERCE.

DEAR COLLEAGUE: The attached report of the Subcommittee on Oversight and Investigations reviews the negative impact on American companies and their stockholders of unfair and confiscatory policies being pursued by the Canadian Government in the energy and investment areas. In view of the large volume of two-way trade between Canada and the United States, which in 1981 exceeded $83 billion, the effect of Canadian initiatives has been to reduce the gross national product of both nations.

The report also documents the weak and ineffectual response of the Reagan Administration to the Canadian programs and singles out Secretary of the Interior James Watt, whose successful efforts to avoid enforcing Federal mineral leasing laws as the Congress intended contributed mightily to the collapse of the Administration's efforts to defend American interests.

The precedent thus established by the Administration can only make it more difficult for the United States to achieve fair and equitable trade relations with Japan and nations in Western Europe.

Sincerely,

JOHN D. DINGELL,
Chairman.

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IMPACT OF CANADIAN ENERGY AND INVESTMENT POLICIES ON U.S. COMMERCE

I. Introduction and Summary

Canada and the United States share a warm, longtime friendship and alliance—a relationship of which both nations are rightfully proud and which has provided both with security, strength and real economic benefits.

We are each other's largest trading partners and that trade plays a very strong role in the economies of both countries. In recent months, however, the economic strength that comes from such trade has been threatened by the restrictive, protectionist policies of the Ottawa Government. These policies have already injured the Canadian economy by driving venture capital from that nation and undermining the value of the Canadian dollar. If continued, the policies will be even more damaging to the economic health of Canada when new capital to create jobs by building new, or expanding existing, industries is not invested because investors have come to believe that Canada simply cannot be trusted. For example, Joseph E. Seagram & Co. has already refused to repatriate to Canada upwards of $4 billion in capital from the sale of U.S. assets because of the Federal Canadian government's policies, and the exodus of Canadian drilling rigs in response to Canada's recent energy policies is well-known.

The record shows that development of energy resources in Canada is falling off, the Canadian dollar is weaker, Canada's economic growth is being retarded, and jobs are being exported to the United States. The Canadian Government is now predicting a 2 percent decline in real output for the fiscal year ending March 31, 1983—the sharpest year-to-year drop since the Great Depression—with a record $19.55 billion budget deficit which would be equivalent to a $155 billion deficit in an economy the size of the U.S.[1] All this means a reduced standard of living in both countries (although less so for the U.S.) and a serious injury to a friendship unique between nations.

As for the impact of these policies on U.S. companies, the sworn testimony of a number of representatives from Executive Branch agencies as well as private corporations is that Canadian investment and energy policies are having a strongly adverse impact on the Canadian subsidiaries of U.S. corporations. This negative impact is, in turn, being felt by the U.S. parent corporations and their stockholders. Although Ottawa's policies are ostensibly intended to encourage increased investment in natural resources by

[1] Wall Street Journal, June 29, 1982.

Canadians while limiting or prohibiting foreign investment, they actually served in the spring and summer of 1981 to encourage a series of takeover attempts by Canadian firms of U.S. companies. The effect of these restrictive Canadian government investment policies is that U.S. firms are denied a fair and equal opportunity to defend themselves against tender offers made by Canadian corporations. Although the bill (H.R. 4145) which the House passed on October 18, 1981, would have eased this problem by applying the same borrowing limits to foreign purchasers as apply to U.S. purchasers of stock in U.S. companies, the Administration actively opposed the measure and the Senate has not acted on it.

As implemented by the Foreign Investment Review Agency (FIRA), Canadian policies have also tended to depress the value of the assets of the subsidiaries of U.S. companies in Canada—at least so long as the assets are acquired by non-Canadian purchasers. The FIRA has also affected the domestic commercial transactions of U.S. corporations on several occasions by refusing to allow the transfer of ownership of the Canadian subsidiary of one American company that has merged with another. The stated rationale for limiting or, in a growing number of cases, preventing the continued flow of foreign investment capital into Canada has been a desire to increase the level of Canadian ownership in certain industries. Despite the fact that foreign capital has enabled the Canadian economy to develop far beyond levels attainable using only domestic resources, and the further fact that on a per capita basis Canadian investment in the U.S. is larger than U.S. investment in Canada, the Trudeau Government has pushed ahead with its discriminatory policies. Paradoxically, while these programs have reduced the inflow of foreign investment, they appear to have significantly increased the outflow of Canadian capital, at least to the United States. For example, the Philadelphia Inquirer reported on September 20, 1981 that in the second quarter of 1981, about $4 billion of Canadian capital was invested in the U.S.—about ten times the normal amount. The Oversight Subcommittee does not take issue with Canadian investment in the U.S. per se, but does object to such investment under conditions and circumstances that are patently unfair and inequitable, which is exactly the case created in industries where the FIRA blocks or severely limits foreign investment.

Unfortunately, despite the efforts by the Office of the U.S. Trade Representative and our Departments of State and Commerce to sound the alarm, the White House has refused to take the Canadian problem seriously. While American companies were fighting for their corporate lives or engaged in protracted negotiations with the FIRA, the White House appeared to be primarily concerned with maintaining the appearance of good relations with Canada at the head-of-state level. Only last fall, after strong pressure from the Congress and in response to a broad public awareness that the takeover situation was running out of control, did the Administration set in motion a bureaucratic process to attempt to develop a coherent and effective policy. But it was the disastrous economic results of its energy and investment programs—rather than any effective response from the Reagan Administration—that persuaded the Trudeau Government to begin to modify its policies. Remarks

of leading Canadian officials, coincident with the new budget introduced in Parliament on June 28, 1982, suggest that the pace of Canadianization in the petroleum sector will slacken.

This future prospect will do precious little to cheer the companies that have already run the gauntlet of a hostile FIRA, defended themselves against a takeover attempt or sold their Canadian assets which were significantly devalued by Canadian policies. As the result of the precedential September 1, 1981 agreement between Ottawa and the energy rich Province of Alberta regarding energy prices and taxation, the Administration lost a golden opportunity to influence Federal energy policy in Canada while it was still in its formative stage.

The failure of this Administration to act quickly and forcefully to defend U.S. national interests will now make it much more difficult to dislodge the Trudeau Government from its protectionist stance. Nonetheless, the U.S. must, either through persuasion or stronger measures, now convince Ottawa to modify its restrictive investment and confiscatory energy policies. To do any less would be to invite other countries to take economic advantage of the U.S. in the trade and investment area. As the world's foremost trading nation, this would be disastrous for the United States.

A good portion of the blame for the delay in responding effectively and forcefully to discriminatory Canadian policies must also be laid at the doorstep of the Secretary of the Interior, James Watt. As evidenced by the record of the hearing of the Subcommittee on Oversight and Investigations on August 6, 1981, the Department of the Interior has been derelict in enforcing provisions of the Mineral Lands Leasing Act (MLLA) which would have protected most U.S. energy corporations from unfair Canadian takeovers. Moreover, by failing for many months to comply with the Subcommittee's request for MLLA information in the possession of the Department of Interior, the Administration frustrated an effort by a committee of the Congress to inform itself fully and completely on issues of pending legislation. The cessation of takeover attempts, at least for the time being, because of economic conditions in Canada and a disinclination by the Trudeau Government to allow Canadian banks to tie up scarce capital in takeover efforts, in no way excuses Secretary Watt.

Even though the crisis atmosphere has passed, the issues of foreign investment, margin laws and resource leasing are troubling national problems that remain before the Congress. The acquisition of Santa Fe International by the Kuwait National Oil Company and the denial by the British Monopolies and Mergers Board of an application by Enserch Corporation to take over the Davy Corporation illustrate the pendency of these issues. Furthermore, the Administration's actions added a new issue to the Congressional agenda. Secretary Watt's failure to comply with a subpoena of a committee of competent jurisdiction at the direction of the President, who invoked a broad claim of executive privilege, provoked a Constitutional confrontation between the White House and the Congress. When faced with the threat of a contempt citation by the House, the President finally made the documents available for inspection by the Members of the Subcommittee on Oversight and

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Investigations.[1a] If the Administration had opposed unfair Canadian policies with the same tenacity with which it resisted a legitimate information request by the Congress on the implementation of the Mineral Lands Leasing Act, American companies with Canadian subsidiaries and their stockholders would likely be better off today.

II. Findings and Recommendations

In 1981, the Oversight Subcommittee held three days of public hearings on the impact of Canadian investment and energy policies. The dates of the hearings and the witnesses were:

JUNE 19

Mr. George Ball, partner, Lehman Brothers; Mr. Samuel Schwartz, Senior Vice President, Conoco; Mr. Philip Wood, Executive Vice President for Finance and Administration, Cities Service Company; Mr. Charles Carlisle, Vice President, St. Joe Minerals Corporation.

JULY 9

Dr. Beryl W. Sprinkel, Under Secretary of the Treasury for Monetary Affairs; Ambassador Robert D. Hormats, Assistant Secretary of State, Bureau of Economic and Business Affairs; Ambassador David R. Macdonald, Deputy United States Trade Representative.

AUGUST 6

Honorable James G. Watt, Secretary of the Interior; Mr. Jack Campbell, Special Assistant to the Assistant Secretary for Policy.

In addition to several statements received for the record from interested companies, the Subcommittee has taken note of various other Congressional hearings and voluminous press coverage on the general subject. Based on all the above information, the Subcommittee makes the following findings:

The Canadian Government, through the actions of its Foreign Investment Review Agency (FIRA) and its National Energy Program (NEP), is pursuing policies that are discriminatory and unfair to American and other foreign mercantile interests in Canada;

The impact of the FIRA and the NEP has been to reduce the current value of Canadian assets owned by U.S. corporations, particularly in the natural resources area, by limiting their future earnings prospects and their corporate flexibility;

FIRA has and will continue to interfere in the commercial activities of American corporations with Canadian assets, even when these activities are primarily concerned with assets in the United States;

The theoretical basis of the NEP fails to differentiate between foreign equity ownership and actual control over company exploration and development operations, which resides with Ottawa and the provincial governments;

[1a] A detailed accounting of this matter is being published by the Energy and Commerce Committee as a separate report.

Despite the discriminatory Canadian policies, which on their face violate the national treatment principles of the Organization for Economic Cooperation and Development as well as Article III of the General Agreement on Trade and Tariffs, the White House was at least initially concerned more with the form rather than the substance of U.S.-Canadian relations;

As a result of the Administration's failure to move in a timely fashion, the U.S. lost its opportunity to modify the objectionable elements of Canadian policy through persuasion and quiet diplomacy. The September 1, 1981 agreement on energy pricing and taxes between Alberta and Ottawa has now solidified the NEP, the main elements of which were passed by Parliament in December 1981;

The snail-like pace of the Department of the Interior's review of whether or not Canadians could qualify to own interests in Federal mineral leases compounded the Administration's weak and uncoordinated response to unfair Canadian Government policies;

State Department cables clearly illustrate that Secretary Watt had prejudged the reciprocity issue in favor of granting Federal mineral leases to foreign parties. Furthermore, he knowingly misled the Subcommittee as to his objectivity on the issue;

After Congressional prodding, the Administration belatedly initiated a major review to develop a coherent policy response to the Canadian problem. A case was also finally brought under the provisions of the General Agreement on Tariffs and Trade (GATT). Formal consultations between the U.S. and Canada in Geneva in February 1982 failed to resolve differences and the Administration has asked the GATT council to establish a panel to hear the charges and issue a formal ruling.[2] The process could take a year to complete. However, any near-term modification to the thrust of Ottawa's protectionist policies is likely to be achieved only through highly coercive economic measures which, in the short run at least, will probably intensify nationalistic feelings in Canada; nonetheless,

The ultimate cost to the U.S. of continuing to turn a blind eye to discriminatory Canadian economic policies is likely to be much greater than any disruption in bilateral relations or trade, because if Canada is allowed to get away with such policies, other nations are sure to follow. Indeed, if a developed nation such as Canada does not have to comply with the national treatment principle, how can the U.S. object to protectionist policies in developing nations in Africa, Asia and the Americas?

Thus, the Subcommittee makes the following recommendations:

1. The Administration should make clear its determination at the very highest level to defend American economic and trade interests against protectionist Canadian policies. In bringing up the economic issue in his meeting with Prime Minister Trudeau on September 17, 1981 President Reagan took a long overdue, if inadequate, step in the right direction.

2. The Administration should immediately set in motion the mechanisms necessary to retaliate under Section 301 of the Trade Expansion Act.

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[2] Wall Street Journal, Mar. 30, 1982.

3. The Administration should not strictly limit its policy review to options of retaliation in kind, but should view the Canadian actions in the total context of bilateral relations.

4. To promote fair and equal competition, legislation bringing purchases of U.S. securities by foreigners under the margin requirements set by the Federal Reserve should be promptly enacted. At present, margin rules limiting stock purchases on credit apply only to U.S. purchasers.

5. The Department of the Interior should return to the practice of earlier Administrations and create a list of reciprocal countries, whose citizens are eligible to own interests in Federal mineral leases issued in accordance with the Mineral Lands Leasing Act of 1920. Countries should be eligible for inclusion on this list only after careful review of their relevant laws and customs. Countries not on the list should be considered as non-reciprocal.

CHAPTER ONE

FIRA AND THE NEP: THE RISE OF CANADIAN PROTECTIONISM

The problems encountered by American companies or their Canadian subsidiaries doing business in Canada stem primarily from the interaction of the Canadian Foreign Investment Review Agency (FIRA) and the National Energy Program (NEP).

Nearly a decade old, the FIRA has only recently been strictly enforced

The FIRA, created by an act of Parliament in December 1973,[3] regulates direct foreign investment in Canada. Under the terms of the Act, foreigners may obtain control over existing businesses or establish new businesses only if such actions are judged "likely to be of significant benefit to Canada." The law describes a number of factors to be taken into account in the assessments including the effect on employment, on exports, on the degree of Canadian participation, and on competition and compatibility with national or provincial industrial or economic policies. There is a rebuttable presumption that acquisition of 5 percent or more of the shares of a publicly traded corporation constitutes control. The applications are reviewed by the Foreign Investment Review Board, which makes a recommendation to the Governor in Council through the appropriate Cabinet Minister. The final decision rests with the Cabinet.

The FIRA was not immediately utilized to deny significant volumes of foreign investment. In the last few years, however, the FIRA has become an increasingly active instrument in a growing wave of Canadian economic nationalism.

The FIRA acts as it sees fit to extract concessions from foreign applicants

The FIRA reaches its decisions with little regard to due process or standard administrative procedure. Assigning weight to the several decisional factors as its sees fit and operating largely in secrecy, the FIRA does as it pleases. According to Assistant Secretary of State Hormats:

> In contrast to the relative openness to which companies are accustomed in the U.S. and elsewhere, U.S. companies have complained to us that FIRA can sometimes be unfathomable in its procedures. Once filed, applications are reviewed confidentially and decisions are handed down with little or no explanation. While there is some opportunity for negotiation, there is little openness in FIRA operations.[4]

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[3] 21-22 Elizabeth II, ch. 46, 619.

[4] "Impact of Canadian Investment and Energy Policies on U.S. Commerce," hearings before the Subcommittee on Oversight and Investigations and the Subcommittee on Telecommunications, Consumer Protection and Finance of the Committee on Energy and Commerce, 97th Congress, 1st session, June 19, July 9 and Aug. 6, 1981, serial No. 97-41, p. 322. Hereinafter cited as Hearings.

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Moreover, FIRA applications often languish while Canadian authorities attempt to extort concessions from the applicants regarding such things as increasing exports or the degree of Canadian ownership. Under the circumstances, the applicants have no recourse save to agree or withdraw their applications. While Canadian officials asserted throughout 1981 that the ultimate approval rate by FIRA was 90 percent, the rate for the fourth quarter of 1980 was only 72 percent.[5] However, this figure ignores the number of concessions extracted and the investors who withdrew their applications or did not apply at all because they knew there was little or no chance of approval.

The FIRA has adversely affected U.S. companies

By its actions, the FIRA has clearly had a significant impact on the activities of U.S. corporations. Effectively, Canada's economic nationalism penalizes U.S. companies with Canadian holdings and gives Canadian purchasers the obvious advantage in what can only be characterized as a buyer's market The NEP comes on top of the impact of the FIRA and singles out for double jeopardy U.S. companies with petroleum or other natural resources holdings in Canada. In 1980, for example, Great Basins Petroleum Company was prevented from selling out to Phillips Petroleum because the FIRA insisted that Phillips sell half of Great Basins' Canadian holdings to Canadians. Phillips cancelled the deal. Saddled with a large amount of debt, Great Basins could not afford to shop around. Commenting on the subsequent sale to United Canso Oil and Gas Ltd., a Canadian company, the senior vice president of Great Basins said "* * * we know we got less than we would have from Phillips * * *."[6]

The Great Basins case is by no means atypical. FIRA has, on several occasions, prevented the transfer by sale of the Canadian assets of one U.S. corporation to another. This is exactly what happened to Amoco Minerals Co., which has not invited bids for its 63% interest in Cyprus Anvil Mining Corporation of Vancouver, British Columbia[7] Amoco obtained its interest in Cyprus Anvil when it bought Cyprus Mines, an American company, in September 1979. Protracted negotiations between Amoco and the FIRA failed to produce an acceptable solution and Amoco was in effect forced to sell out to Canadians. Press accounts indicate that the Mobil Oil Corporation and The Getty Oil Corporation are experiencing similar frustrations with the FIRA regarding the Canadian subsidiaries of U.S. companies they acquired.[8]

FIRA's reach extends far beyond energy companies

FIRA denial of U.S. investment is by no means limited to the natural resources area. A case in point involves two American food processing companies, McCormick and Company of Hunt Valley, Maryland and the Stange Company of Chicago. McCormick acquired Stange in February 1981, but the FIRA refused to allow

[5] Hearing pp. 321-2. See also FIRA quarterly report, October-December 1980, p. 2
[6] Business Week, June 8, 1981, p. 71.
[7] Wall Street Journal, July 10, 1981.
[8] For Mobil, see the Wall Street Journal, Sept. 25, 1981; for Getty, see the New York Times, Apr. 6, 1981.

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McCormick to assume control over Stange's Canadian subsidiary.[9] In another recent ruling, the FIRA rejected a bid by Angelica Whitewear Ltd., a non-Canadian company, to acquire the Service Uniform Company.[10] Gannett Co., a large newspaper publisher based in Rochester, N.Y., was permitted by FIRA to purchase a large Canadian billboard company only after agreeing to purchase substantial volumes of Canadian newsprint for its U.S. operations, and Apple Computer of California similarly was allowed to establish operations in Canada only after agreeing to purchase Canadian made parts and to recommend Canadian made equipment to its dealers around the world.[11] Such tie-in arrangements by U.S. companies raise serious questions under U.S. antitrust laws.

The FIRA Quarterly Report for the last quarter of 1980 provides other, even more puzzling examples of disapproved investments including proposals to establish a company to develop corn seedstock, to obtain the food service contract at the Windsor Raceway—located in Ontario, just minutes from Detroit—and to open a chain of pizza shops.[12]

[9] Wall Street Journal, June 1, 1981.
[10] Id.
[11] New York Times, Feb. 16, 1982.
[12] FIRA, quarterly report, October–December 1980.

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CHAPTER TWO

THE PROPOSED NATIONAL ENERGY PLAN

Canada's NEP changes the rules well after the game has begun

The NEP was announced by the Trudeau Government on October 28, 1980.[13] One of the primary objectives of the plan was to increase the level of Canadian ownership in the energy industry from its present 28 percent to at least 50 percent by 1990. In the view of the Trudeau Government, such a high degree of foreign ownership of Canadian energy resources is intolerable.[14] This view overlooks the contribution foreign investment has made to the development of the Canadian energy industry as well as the fact that such investment was previously welcomed. Clearly, U.S. investors historically relied upon a neutral investment environment that has now been unilaterally rescinded. According to Mr. Philip Wood, Executive Vice President for Finance of the Cities Service Company:

> The failure to consider fairness to the providers of foreign capital after substantial investments are in place definitely constitutes changing the rules after the game has begun.[15]

Moreover, the theoretical underpinnings of the NEP fail to differentiate between foreign ownership and actual control. Hydrocarbon leasing, drilling, transportation and pricing are all matters under the direct control and regulation of Ottawa and the provincial governments. If foreign companies "own" the majority of the proven reserves, the Canadian authorities tell the companies what they can do, and where and when they can do it.

The large and mutually beneficial flow of trade and investment between Canada and the U.S. is being undermined by Canadian policies

It is hardly surprising that, as a rich and far more populated neighbor, U.S. companies have large investments in Canada. U.S. direct investment in Canada exceeds $40 billion compared to about $7 billion which Canadians have invested in this country.[16] The inflow of investment from the U.S. has enabled Canada to develop its economy to a level that would not have been otherwise possible. In fact, the Canadian economy has developed to a level such that on a per capita basis, Canadian investment in the U.S. is larger than U.S. investment in Canada. Moreover, Canadian investment in the U.S. is growing much more rapidly that U.S. investment in Canada.[17]

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[13] For details, see bill C-48, 1st session, 32d Parliament, 29 Elizabeth II, 1980.

[14] See, for example, "Notes for an Address by Peter M. Towe, Ambassador of Canada, to the Gasmen's Roundtable, National Energy Program, Washington, D.C., July 7, 1981," released by the Public Affairs Division of the Canadian Embassy

[15] Hearings, p. 78.

[16] Hearings, p. 320.

[17] Hearings, opening statement of Assistant Secretary Hormats.

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According to a recent report by the Investment Analysis Division of the Commerce Department's International Trade Administration, Canadians made by far the greatest number of direct investments in the U.S. by foreigners during the period January 1 through June 30, 1981.[18] The report lists 151 Canadian investments compared to 72 by the United Kingdom and 45 by West Germany, the second and third highest numbers respectively. Overall, Canadians accounted for 27.9 percent of the total number of foreign investments during the period. The $4.172 billion value of these investments was more than 46 percent of the total investment cases with known values. Based on the figures for the first half of 1981, the pattern established in previous years is accelerating. In 1979 and 1980, Canada was the number one foreign investor in the U.S.[19] In 1979, Canadians accounted for 17 percent of the total while the figure increased to 21 percent in 1980. The dollar value of Canadian investments has also increased significantly from year to year.

The flow of investment between Canada and the U.S. has been of great benefit to both countries over a period of decades. For Canada now to implement such protectionist policies regarding its most important trading partner is most unfortunate and cannot be to the ultimate benefit of either country.

The NEP is heavily biased in favor of Canadian companies

The draft NEP contained a complex set of taxes and incentives heavily weighted in favor of companies that qualified as majority-owned and controlled by Canadians. Generally speaking, the NEP phases out the depletion allowance in favor of a system of government cash grants for exploration and development. Although non-Canadian companies can qualify for some payments, the grants are scaled upward over time greatly to favor Canadian owned and controlled companies. For example, a 50 percent Canadian owned firm would receive payment equal to 35 percent of allowable expenses for exploration in frontier areas (known as Canada Lands), and a 75 percent Canadian owned firm would be reimbursed for 80 percent of allowed expenses. A foreign-owned firm would get a 25 percent payment.[20]

A February 1981 study by the investment banking house of Salomon Brothers illustrates the net effect of the tax/grant package.[21] After taxes, a 75 percent Canadian owned firm could spend $1.00 on frontier exploration by contributing only about $.08 of its own cash. A comparable investment by a non-Canadian company would require $.28 of that company's funds, or over three times as much. Over all, Salomon Brothers concluded that a firm controlled and 75 percent owned by Canadians might enjoy 25 percent more earnings and 15 percent more cash flow than a foreign firm.

Well before it became law, the proposed NEP clearly illustrated the intent and direction of the Trudeau Government's energy

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[18] "January-June 1981. Transactions Activity", Investment Analysis Division, Office of International Investment, U.S. Department of Commerce, December 1981.

[19] "Foreign Direct Investment in the U.S., 1980 Transactions," International Trade Administration, U.S. Department of Commerce, October 1981.

[20] See "The National Energy Program 1980," prepared by the Canadian Ministry of Energy, Mines and Resources.

[21] Picchi, Bernard J., "The National Energy Program of Canada: Causes and Effects," New York: Salomon Brothers, February 1981.

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policy. Once it was announced, the future earnings prospects of non-Canadian companies, most of which are American owned, were immediately diminished. The market price of the Canadian subsidiaries of American energy companies fell sharply.

Contributing to the overall anti-foreign atmosphere were two particularly onerous provisions of the NEP. The first specified Canadian source requirements for equipment and services for petroleum exploration and development. This proposal was blatantly violative of the General Agreement on Tariffs and Trade, the major international agreement governing trade and tariff barriers among Western trading nations. Following sharp protests from the U.S. Trade Representative and the Department of State, the Canadian Government "clarified" the plan so that no company would be required to purchase Canadian goods and services if they were not competitively priced.[22]

The second proposal was that the government acquire a 25 percent share of oil and gas production revenues, essentially without compensation. The initiative was also made partially retroactive. Some modification in terms of limited compensation was made in response to strong protests from the companies,[23] but the modified proposal in no way compensates fully the companies for their actual expenditures.

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[22] Hearings, prepared statement of Assistant Secretary Hormats.

[23] Id. See also the remarks by the Honorable Mark Lalond to the House of Commons Standing Committee on National Resources and Public Works, May 14, 1981.

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CHAPTER THREE

THE TAKEOVER SYNDROME

The NEP precipitated a wave of takeover attempts

The relative attractiveness of U.S. companies, especially in the natural resources area, combined with the negative reaction of many Canadian investors and companies to the proposed NEP[24] precipitated a spate of acquisition efforts directed towards U.S. companies or their now vulnerable Canadian subsidiaries. In early 1981, Zale Corporation, a Dallas jewelry company, the Hobart Company of Ohio and the investment firm of Bache & Company were all the targets of takeover attempts by Canadian firms. The fact that in each case the U.S. corporation was able to reach an alternative agreement with another U.S. company does not obscure the fact that none of the mergers was voluntary or even desired. Moreover, on September 12, 1981, the New York Times reported that Bache Halsey Stuart Canada Ltd., which was acquired by Prudential Insurance, had been denied continued membership on the Toronto Stock Exchange. Because of the acquisition of its parent by Prudential, Bache Canada had to reapply for membership and ran afoul of Ontario rules that require securities firms to be no more than 25 percent controlled by nonresidents. If Bache's appeals to Ontario courts are denied, the firm would be forced either to give up its seat on the Toronto Exchange or merge with Canadian firms in a manner that would satisfy Canadian ownership requirements.

Furthermore, Prudential's FIRA application is still pending, which suggests that the FIRA is also attempting to extract concessions regarding the degree of Canadian ownership.

St. Joe Minerals loses its Canadian assets

In March 1981, Joseph Seagram & Co. made a tender offer for St. Joe Minerals Corporation. The dilemma posed to St. Joe's by the Seagram offer graphically illustrates how the NEP and the FIRA have combined to the disadvantage of U.S. companies, particularly those in the natural resources field. As pointed out in testimony before the Subcommittee,[25] the FIRA has already incorporated the "Canadianization" aspects of the proposed NEP into its review process. As a practical matter, the FIRA no longer allows the sale of any Canadian corporate assets in the natural resources area to non-Canadians. In the case of St. Joe, which owned 92 percent of CanDel, an attractive Canadian oil and gas subsidiary, the Canadian assets suddenly became a liability in attempting to resist Sea-

[24] See hearings, statement of Deputy USTR Macdonald; also "Submission to the National Energy Board Hearing on Energy Supply and Demand," vol. 3, Canadian Petroleum Association, January 1981.

[25] Hearings, p. 287.

gram's offer. St. Joe could not hope to attract a better offer from an American firm so long as it owned CanDel because the FIRA would disallow the sale or even the transfer of CanDel to a non-Canadian company. St. Joe was able to arrange a quick sale of CanDel to Sulpetro, a Canadian company, and attract a bid of $60 per share from Fluor Corporation. Seagrams, obviously seeking to take advantage of the opportunity created by Canadian Government policy, had bid only $45 per share for St. Joe, including the CanDel assets.

Conoco forced to sell Canadian petroleum company to Dome

An even more graphic example of the inequities created by Ottawa is the raid on Conoco by Dome Petroleum Ltd. of Calgary. In early May 1981, Dome announced its intent to acquire Hudson's Bay Oil and Gas Co., a Canadian company that was 52.9 percent owned by Conoco. Dome's strategy, which was successfully realized on June 2, was to make a tender offer for up to 22 million shares of Conoco's common stock and then to trade it for Conoco's interest in Hudson's Bay. Although Conoco, the 14th largest corporation in the U.S., had no desire to sell Hudson's Bay and attempted to resist Dome's overtures, they had little choice in the end but to agree. According to Mr. Samuel Schwartz, Senior Vice President of Conoco, the NEP had depressed the market price of Hudson's Bay and the FIRA blocked any non-Canadian competitive bidding for the company. It also prevented Conoco from defending itself by virtue of a counter tender offer for the shares of Dome. Concluded Mr. Schwartz: "The bargaining advantage, therefore, was clearly tilted in favor of Dome due to Canadian Government policy."[26]

Nu West's raid on Cities Service illustrates inequities in securities law

Later that same month, another Canadian company, Nu West Group Ltd., attempted what appeared to be an instant replay of the Dome tactic. Nu West revealed that it had purchased about $250 million worth (over 5 percent) of the common stock of Cities Service Company of Tulsa. Analysts immediately speculated that Nu West would attempt to swap the stock for equity in Cities' wholly owned Canadian subsidiary. The circumstances of the stock purchase, as revealed in Nu West's filings with the Securities and Exchange Commission, were extraordinary. The loan used to purchase the stock, which was obtained from the Toronto Dominion Bank, exceeded the net worth of Nu West while the $60 million annual interest payment was greater than the $57 million profit earned by Nu West for all of 1980. A U.S. corporation would have been prohibited by Federal Reserve Board margin requirements from launching such an irresponsibly speculative effort.

On October 13, 1981 the House passed H.R. 4145.[27] a bill unanimously approved by the Energy and Commerce Committee, which would make foreign purchasers of stock in U.S. companies meet the same margin requirements as apply to U.S. purchases. At present, the Federal Reserve Board limits the amount of money that

[26] Id., p. 107.
[27] See Congressional Record, Oct. 13, 1981, pp. H7207-7210.

can be borrowed to buy securities to 50 percent of their value if the stock is used as collateral for the loan. The bill was designed to prevent the type of rank speculation attempted by Nu West while creating equality of treatment for all investors in the U.S. securities market. Unfortunately and inexplicably, there was opposition to the bill from the Administration and the measure has been blocked in the Senate.

Cities Service refused to exchange any of its estimated $500 million worth of Canadian assets for the shares of it common stock acquired by Nu West, apparently preferring for the short term to attempt to live with the fact that its largest stockholder probably had interest hostile to, or at least inconsistent with, those of the corporate management. At a minimum, Nu West's action disrupted Cities Service's corporate planning. However, on September 21, 1981, Cities Service announced that it had reached agreement with Nu West to buy back its stock. The company paid $51 per share for the 6.02 million shares, or almost $73 million more than the market price for those shares which closed that day on the New York Stock Exchange at 38⅞. [28] In four months, Nu West was able to rack up a net profit on its purchase of Cities Service of $35 million.

Du Pont acquires a weakened Conoco

Even while Cities Service and Nu West was trading salvos, Seagrams launched a new effort, in this instance an attempt to acquire a controlling interest in the embattled Conoco. After a spirited bidding war that was overshadowed on the front pages only by the Royal Wedding, Du Pont defeated both Mobil and Seagrams.

The Conoco merger and the rumors that others were imminent generated intense speculative trading on the U.S. stock markets and led to the establishment of lines of credit running into the tens of billions of dollars for potential corporate takeovers or defensive operations. While tieing up scarce credit resources in non-productive uses and threatening to overwhelm antitrust laws, the spectacular maneuvers failed to produce so much as an extra drop of oil on either side of the U.S.-Canadian border.

Canadian takeovers transfer resource ownership from U.S. hands

One concrete effect, however, is that the sales by St. Joe and Conoco have unfairly transferred prime oil and gas acreage outside the borders of Canada from U.S. companies into the hands of Canadian companies. Hudson's Bay had 10,575 acres under lease in Egypt, Indonesia, Australia, Brazil and other countries while CanDel had a 14 percent interest in property adjacent to a major oil find by Texaco in the North Sea. Such transfers are in addition to the sales or proposed sales to Canadians of the petroleum assets of the Canadian subsidiaries of U.S. corporations. Examples include Marathon's announcement on September 8, 1981 that because of disincentives under the NEP, it was considering selling its two Canadian oil and gas subsidiaries, Marathon Petroleum Canada Ltd. and Pan Ocean Oil Ltd.[29] The two companies have estimated net

[28] New York Times, Sept. 21, 1981.
[29] New York Times, Sept. 9, 1981.

reserves of 17 million barrels of oil and 249 billion cubic feet of natural gas along with nearly 550,000 net exploratory acres. The sale was completed in February 1982 to Aberford Resources Ltd. of Calgary.[30]

These figures pale in comparison to the assets of Union Oil of Canada. Union Oil of California, the parent company, has made a tender offer to purchase the outstanding shares of Union of Canada to allow the subsequent sale of the company's conventional petroleum reserves. Union estimates gross proven reserves in Canada at year end 1980 of about 92 million barrels of oil and over 600 billion cubic feet of natural gas, with a net exploratory acreage of almost 3.3 million.[31]

The NEP has disrupted expansion of the energy sector in Canada

While such sales increase the percentage of Canadian ownership in that country's petroleum sector, they do not result in the discovery of any new reserves. In fact, the NEP has significantly reduced capital expenditures for petroleum exploration in Canada by U.S. owned companies below planned levels and disrupted the industry generally.[32]

According to figures recently complied by the Canadian Petroleum Association,[33] the trade group for the major domestic and foreign companies operating in Canada and an outspoken opponent of the NEP, any realistic hope of attaining the goal of Canadian energy self-sufficiency by 1990 has been lost because of the NEP. The Association charged that 15,000 direct jobs in the petroleum industry had been lost, drilling completions had declined 22 percent in 1981 and more than 300 drilling rigs had left Canada. After 18 months, the program had reduced foreign ownership in the petroleum industry by 4.5 percentage points to about 66 percent, but at a cost of over 7 billion dollars (Canadian).

Moreover, several large synthetic fuel projects that were counted on to provide an economic stimulus as well as a significant portion of Canadian crude oil by the end of the decade have been scrapped. Last year, Imperial Oil shelved a $12 billion synthetic crude project at Cold Lake, Alberta. On April 30, 1982 the Alsands Consortium announced the cancellation of that $13 billion oil sands effort.[34] The Alsands development was projected to produce 137,000 barrels of synthetic crude oil per day, about 10 percent of Canada's current crude production. The Alsands announcement came the same day—now referred to by some as "Black Friday"—that a two year delay in the $37 billion Alaska Natural Gas Pipeline was revealed.[34a] The cancellation or deferral of these massive proposals has called into question the Trudeau Government's entire economic strategy.

Although there has been a respite on takeovers by Canadian companies—apparently due in large measure to pressure from Ottawa on Canadian lending institutions in an effort to halt the

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[30] Wall Street Journal, Feb. 16, 1982.
[31] See Union's prospectus, June 16, 1981, p. 11.
[32] See hearings, exhibit 1, p. 214.
[33] New York Times, Apr. 30, 1982.
[34] Wall Street Journal, May 3, 1982.
[34a] Washington Post, May 8, 1982.

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plunge of the Canadian dollar—the essential conditions that produced to takeover syndrome have been masked rather than eradicated.

Elf's takeover of Texasgulf the indirect result of the NEP

Canadian policies also caused the takeover of a U.S. company, Texasgulf, by Elf Aquitaine, a French energy company 67 percent owned by the French Government.[35] As a non-Canadian controlled company, Elf was put at a disadvantage by the NEP just as U.S. companies were. In the summer of 1981, Elf in effect traded its Canadian assets to the Canada Development Corporation, controlled by Ottawa, and received the 37 percent of Texasgulf's shares held by CDC. Elf also acquired the remaining Texasgulf stock via a tender offer. While the complex 5.1 billion dollar transaction was beneficial to the French and the Canadian Governments, the dismemberment of Texasgulf resulted in the transfer from American hands of valuable minerals including the Kidd Creek mine, containing silver, copper, zinc, lead and cadmium and considered by some as the richest single mine in the world. Elf is now joining in the competition for U.S. petroleum reserves. According to Elf's chariman, he plans to build "a little French Exxon."[36]

[35] Wall Street Journal, June 29, 1981.
[36] Business Week, March 8, 1982.

CHAPTER FOUR

THE FAILURE OF THE REAGAN ADMINISTRATION

The White House ignored the warnings from concerned agencies while Canadian policies were being formulated

The Administration's response to the threat to American interests of Canadian investment and energy policies has been tardy and ineffectual. The best efforts of the Office of the U.S. Trade Representative (USTR), the Department of State and, finally, the Department of Commerce to capture the attention of the White House and to enlist the support of senior administration officials, which was necessary to deal effectively with the Canadian Government, fell on deaf ears for many months. The new Administration seemed more concerned with atmospherics, preferring a seeming aura of good feeling to the task of confronting the troubling realities of U.S.-Canadian economic relations. As a result, Ottawa's policy as embodied in the September 1, 1981 [37] agreement on energy prices and taxes with Alberta, has now jelled. Whatever opportunity existed to modify the NEP through quiet diplomacy so that Canadian national goals could be pursued by methods that were less injurious to U.S. economic interests has passed.

Significant alterations in Canadian policies can be achieved now only by employing highly coercive initiatives that run the very real risk of precipitating an even stronger nationalistic reaction in Canada and increasing the protectionist sentiment. In short, more than nine months of benign neglect by the White House only made the situation more difficult to resolve and potentially more disruptive to continued mutually beneficial trade relationships.

The contrast between the strong representations of the USTR and the complacent attitude of senior Administration officials is clearly visible in the record of the Subcommittee's hearing on July 9, 1981.[38]

By withdrawing a diplomatic note, the White House undermined U.S. diplomats

As recorded in the chronology attached to the testimony of Deputy USTR Macdonald, officials from the Office of the USTR and the Departments of State and Commerce had been expressing the serious concerns of the U.S. government to Canadian officials regarding the FIRA in meetings and in diplomatic notes since at least April 1980. Less than a month after the announcement of the proposed NEP, U.S. officials met with their Canadian counterparts in Ottawa to initiate formal bilateral discussions on that subject.

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[37] See "Summary, Canada/Alberta Memorandum of Agreement on Energy Pricing and Taxation," Sept. 1, 1981, Public Affairs Division, Canadian Embassy, Washington, D.C.

[38] Hearings, see especially the statement of Deputy USTR Macdonald.

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The credibility of these representations was undermined, however, by the actions of the new Administration. Just prior to President Reagan's initial visit to Ottawa, the Department of State on March 5, 1981 delivered a strongly-worded note to the Canadian Government reiterating U.S. concerns over the NEP's trade, investment and energy provisions. The timing of the note, which was fully coordinated among the various Executive Branch agencies concerned, would have placed the new Administration firmly behind efforts to persuade Ottawa to modify its objectionable policies. Instead, on March 9, the note was withdrawn.[39] According to Assistant Secretary of State Hormats, this was: "* * * because of the tone of the note and the concerns that it raised prior to the visit of the President to Ottawa."[40]

When asked by Congressman Synar why this was not taken into account before the note was sent, the Assistant Secretary could only respond that "* * * in retrospect it should not have been sent."[41]

In the context of previous U.S. protests, the withdrawal of the note sent quite the opposite message to the Trudeau Government. It was abundantly clear that the White House did not have any strong feelings on the issues raised by the actions of the FIRA and the proposed NEP. The withdrawal of the note reduced the impact of subsequent U.S. protests, as expressed in meetings and further written communications between April and the end of June, to *pro forma* exercises that could be ignored effectively. Indeed, the Canadian Embassy in Washington did not even bother to forward to Ottawa an *aide memoire* that was passed to them on April 3 by the Department of State of behalf of the U.S. Government.[42]

Congress reacts strongly to Canadian policies and administration inaction

The Canadian Government was also keenly aware of mounting Congressional criticism of Canadian policies and Administration inaction. In addition to a growing volume of media attention on the merger phenomena, Canadian diplomats monitored actively the mood on Capitol Hill, where several pieces of punitive legislation has been introduced. Canadian concerns were high because of the Economic Summit[43] scheduled to convene in Ottawa in late July 1981 and the fear that the U.S. might embarrass Prime Minister Trudeau by forcefully raising the issue of Canadian protectionism. Because Canadian policies also threatened other Western trading nations and Japan, which would be present at the meeting, the Congress began to press the White House to take up the issue at the Summit. On June 24, Congressmen Dingell and Broyhill, the Chairman and Ranking Minority Member of the Committee on Energy and Commerce, jointly sent a letter to the President expressing their concerns over the impact of Canadian policies and urging the President to accord the issue high priority at the

[39] Id., p. 331.
[40] Id.
[41] Id.
[42] Id., p. 332. See also the chronology appended to the statement of Deputy USTR Macdonald.
[43] This meeting was attended by the Heads of State and the Finance Ministers or their equivalent of Canada, the United States, Great Britain, France, Italy, West Germany and Japan.

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Summit.[44] Furthermore, in his capacity as Chairman of the Subcommittee on Oversight and Investigations, Congressman Dingell convened a hearing on July 9 to examine further this matter.

Representing the Administration at the hearing were Dr. Beryl Sprinkel, Under Secretary of the Treasury for Monetary Affairs, Ambassador David Macdonald, Deputy U.S. Trade Representative, and Ambassador Robert D. Hormats, Assistant Secretary of State, Bureau of Economic and Business Affairs. The testimony of all three endorsed the principle that it is desirable U.S. policy to encourage the free flow of investment between countries and to do so is consistent with existing international agreements. They were openly critical of Canadian policies and expressed a growing frustration over the failure to change them through diplomatic efforts. Specifically, Dr. Sprinkel characterized developments in Canada as "quite troublesome",[45] Ambassador Macdonald stated that the policies are "discriminatory in that U.S. and other foreign owned firms" are treated "less favorably than Canadian-owned firms",[46] and Ambassador Hormats described the Canadian policies as "nationalistic and unproductive," adding that he was puzzled at how Canada could expect to have it both ways: "seeking benefits from participating in the Western Industrial Club, while claiming specific rights to promote indigenous development by curtailing certain foreign economic activity."[47]

Ambassador Macdonald further testified that he considered FIRA and the NEP as serious derogations from the 1976 declaration on national treatment of the Organization for Economic Cooperation and Development (OECD) and that certain aspects also contravened Article III of GATT.[48] Notwithstanding the fact that these views were widely shared in the Departments of State and Commerce,[49] and that the OECD itself had criticized the Canadians in March,[50] the Administration had still not come to grips with the issue.

The President fails to press Prime Minister Trudeau at the economic summit

Since President Reagan and Prime Minister Trudeau were scheduled to meet at the White House on July 10 to coordinate their views in advance of the Summit, the Subcommittee was understandably curious whether the President at last would take this opportunity to raise the issue forcefully. Dr. Sprinkel responded that he was not certain, but "certainly would not be surprised if it were brought up in a rather pointed fashion".[51] Ambassador Macdonald added that at a meeting of Cabinet officials interested in the matter, the "unanimous feeling" was that the matter would be brought up.[52] When the witnesses were asked whether or not it

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[44] Printed as app. B.
[45] Hearings, prepared statement of Under Secretary Sprinkel.
[46] Id., prepared statement of Deputy USTR Macdonald.
[47] Id., prepared statement of Assistant Secretary Hormats.
[48] Id., Macdonald statement.
[49] Id., Hormats statement. See also letter from Secretary of Commerce Baldrige to Chairman Dingell, Aug. 31, 1981, printed as app. E.
[50] Washington Post, May 7, 1981. See also Hormats statement.
[51] Hearings, p. 333.
[52] Ibid.

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would be brought up during the Economic Summit the week of July 20, Ambassador Hormats responded that he could not predict precisely what would be discussed, but that it "would not surprise me at all" if the issue of investment performance requirements were raised.[53]

Unfortunately, it is the Subcommittee that ended up not being surprised that the White House let another golden opportunity pass without forcefully pressing the issue. According to an August 26, 1981 letter to Chairman Dingell from Deputy USTR Macdonald, the President merely "noted" U.S. concerns regarding FIRA and the NEP at his July 10 meeting with Prime Minister Trudeau.[54] Ambassador Macdonald added that, to his knowledge, the issue was not brought up at the July 1981 Ottawa Summit, a fact that was subsequently confirmed by Interior Secretary Watt.[55]

The near total failure of the Administration's effort to modify Canadian policy was finally acknowledged by the USTR's Office the next month. In a letter of August 21, 1981, to Chairman Dingell, Deputy USTR Macdonald flatly stated: "To date, as you are undoubtedly aware, our diplomatic efforts to modify the objectional aspects of the NEP and FIRA have achieved only marginal success." [56]

The letter went on to note that on August 13, two subcommittees of the Trade Policy Staff Committee initiated a review to consider in detail the impact on U.S. interests of the FIRA and the NEP and to develop policy options. The review was to be completed in mid-September. The letter said: "The purpose of this review is to develop a response in a systematic and comprehensive manner rather than on an *ad hoc* basis." [57]

In other words, some 10 months after the proposed NEP was announced the Administration had decided that it was high time to try to figure out what to do about it.

The belated nature of the Administration's effort was further underscored by a September 10, 1981, article that appeared on the front page of The Washington Post.[58] The article reported that:

> The Reagan Administration is considering tough retaliatory sanctions against the Canadian government if it goes ahead with nationalization plans aimed at limiting U.S. investment in Canada.[59]

If begun in earnest six months earlier, the review may have caused Ottawa some pause. However, coming as it did more than a week *after* the September 1st announcement of the agreement between Alberta and Ottawa on energy prices and taxes—which for all intents and purposes finalized the basic elements of the NEP—it was unlikely to have any fundamental effect on Ottawa except to confirm in the minds of the Trudeau Government that they were correct in ignoring the protests of the USTR and the Department of State.

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[53] Id., p. 334.
[54] Printed as app. C.
[55] Hearings, p. 362.
[56] Printed as app. D.
[57] The TPSC is an interagency body composed of sub-Cabinet level officials. Its recommendations would normally go to the Trade Policy Committee of the Cabinet.
[58] Washington Post, Sept. 10, 1981.
[59] Id.

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U.S. acquiescence to discriminctory Canadian policies sets bad precedent

While this terrible precedent will certainly complicate the work of our trade and diplomatic personnel in future contacts with Canada, and has now cast a rather uncharacteristic pall over the usually bright status of bilateral relations, the most damaging impact may ultimately be on the perceptions of our other trading partners. As noted by Secretary of Commerce Baldrige in an August 31, 1981 assessment of the Canadian situation:

> Canada's investment policies—which have become increasingly restrictive since the mid-1970's—have been especially troublesome to us . . . Furthermore, because Canada is a major industrialized nation, what it does in the international sphere is likely to give encouragement to others to do the same.[60]

In this regard, it may be only sheer coincidence that the United Kingdom's Monopolies and Mergers Commission, which in March 1981 began a review of an offer by Enserch Corporation of Dallas for Davy Corporation, a London-based engineering and construction concern, announced its disapproval of the bid on September 10. This was so even though a substantial portion of Davy's operations was generated by its acquisition of a U.S. company—McKee.[61]

Token Canadian concessions head off Cabinet threat of sanctions

In mid-October 1981, the Cabinet met to consider possible retaliatory actions against Canada as had been promised in September. However, instead of a decision to apply sanctions, the Cabinet sent Treasury Secretary Donald Regan to Ottawa for yet another round of consultations. According to an unnamed Administration official cited in The Washington Post,[62] the Canadians had been upset by the September announcement that the Administration was considering sanctions and the Regan trip was designed to "allow the Canadians to make decisions favorable to the United States without being under public pressure from the Administration."

The favorable changes were apparently the Canadian Government's decision (included in the budget presentation to the House of Commons on November 12 by Deputy Prime Minister MacEachen) to put off for the time being the next phase of proposed FIRA action.[63] The Canadian cabinet had been considering giving FIRA the power to monitor the operations of foreign companies in Canada and to extend the Canadianization program far beyond the energy sector. However, the Minister of Energy, Mr. Lalonde, made it clear that the operations of the FIRA and the implementation of the NEP would remain unchanged in the energy area.[64] Thus, in return for a promise not to commit a further injustice, the Reagan Administration in effect decided to accept the injustice already committed.

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[60] See app. E.
[61] Wall Street Journal, Sept. 11, 1981, p. 10.
[62] Washington Post, Oct. 22, 1981.
[63] See "Canadian Budget, Executive Summary," Department of Finance Press Release, Nov. 12, 1981.
[64] New York Times, Sept. 25, 1981.

Phase II of the NEP raises new concerns

The appeasement policy soon bore bitter fruit. On February 26, 1982, the Trudeau Government introduced a massive legislative package, titled the Energy Security Act (ESA), in the House of Commons.[65] The ESA is intended to complete the implementation of the NEP. As introduced, the 149-page bill proposed to amend or enact 13 separate acts and abolish another.[66] The bill was so large that the main opposition party boycotted the House of Commons for over two weeks, bringing the legislature to a halt while the bells that signal a vote continued to ring day and night, until the Trudeau Government finally agreed to split the package into more manageable parts.[67]

Preliminary analysis of the proposed legislative package by the Department of State reveals several potential new problems. As expressed by Assistant Secretary of State Robert Hormats in testimony before a Senate Subcommittee on March 10, 1982[68] the U.S. is concerned over the constrained shares provision in the ESA. The proposal contemplates allowing the forced sale of minority stock holdings in Canadian energy companies if mandated by a two-thirds vote of the holders of that class of shares. The idea is part of the broad effort to increase the degree of Canadian ownership in the petroleum sector and, more specifically, to provide a means whereby Canadian companies could qualify more easily for government exploration grants, which are based in part on the degree of Canadian ownership. However, the scheme is discriminatory on its face against minority shareholders and could depress further the price of energy stock in foreign hands. The proposal could also run afoul of the Securities and Exchange Commission or state laws protecting minority stockholders' rights in shares traded on exchanges in the U.S., raising the possibility of delisting Canadian petroleum stocks. There are indications that more responsible elements in the Canadian Government are rethinking this proposal.

Assistant Secretary Hormats noted that the ESA contains "other objectionable provisions" including the Petroleum Incentives Program, which determines the rate of Canadian ownership and thus the amount of government exploration grant. According to the Assistant Secretary: "The Canadian ownership rate rules concern us because they embody an overtly discriminatory regime based on nationality to award financial grants to explore in Canada."[69]

The Assistant Secretary stated further that there was troubling trends emerging from the recently-enacted Canada Oil and Gas Act. This legislation established the Canada Oil and Gas Lands Administration (COGLA) which has begun to plan for the redistribution of existing petroleum rights held by private companies. The State Department has learned that non-Canadian companies may be forced to relinquish large portions of their existing acreage in order to obtain new exploration permits.

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[65] Wall Street Journal, Mar. 18, 1982.
[66] A text of the bill is available in the subcommittee's files.
[67] Wall Street Journal, Mar. 18, 1982.
[68] Statement of Assistant Secretary of State Robert D. Hormats before the Subcommittee on International Economic Policy of the Committee on Foreign Relations, U.S. Senate, Mar. 10, 1982.
[69] Id.

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The first example of this is a recent agreement whereby Imperial Oil Ltd. will give up nearly half its rights to future discoveries on 6 million acres it now holds in the Arctic in order to obtain exploration permits needed to pursue its search for hydrocarbons.[69a] Imperial will be permitted to keep its 86 percent interest in petroleum produced from already discovered reserves but its share will fall to about 47 percent of newly discovered oil and gas. Imperial's interests will be transferred to 11 Canadian companies, who will provide the bulk of the exploration money. Petro-Canada, the state-owned oil company, acquired a 14 percent interest from Imperial several years ago under provisions that allowed a 25 percent stake. Petro-Canada under the latest legislation can take a further 25 percent interest in all petroleum rights on Canada Lands, which includes the Arctic area. Moreover, the COGLA threatens to join with the Committee on Megaprojects, Industrial and Regional Benefits to force "buy Canadian" policies upon energy companies.

When discussing the FIRA, Assistant Secretary Hormats had some bad news. Referring to the November 1981 Canadian budget message, which, as discussed above, promised a review of FIRA activities and the deferral of a planned expansion in the scope of the agency's coverage, he said:

> We were told in the fall that the FIRA was considering adopting a policy of more explicitness and openness in its decisionmaking process—in particular, publicly explaining the reasons for disapprovals. There were also indications that size criteria would be applied, granting small businesses special treatment. While certain of our important concerns would remain, these would be positive steps. We have not, however, seen actual signs of such new policies. Foreign investors continue to face complex and difficult FIRA performance requirements.[70]

Despite discriminatory Canadian policies, the White House appears determined not to insist on equal treatment for U.S. companies. In August of this year, the Congress passed the Bus Regulatory Reform Act of 1982 (Public Law 97-261). Section 6 of this Act imposed a moratorium on the issuance by the Interstate Commerce Commission of operating certificates to motor carriers owned or controlled by Canadian or Mexican interests. The Congress took this action to counter restrictive practices against U.S. motor carriers by the two countries. However, when he signed the legislation into law on September 20, President Reagan sent a memorandum to the U.S. Trade Representative (see the Federal Register, September 22, 1982, p. 41721) suspending the moratorium against Canada.

[69a] Wall Street Journal, May 11, 1982.
[70] Hormats statement, Mar. 10, 1982.

CHAPTER FIVE

THE MINERAL LANDS LEASING ACT: FAILURE BY THE SECRETARY OF THE INTERIOR TO ENFORCE THE LAW

The MLLA: A potential weapon against discriminatory Canadian policies

The remedies for discriminatory Canadian economic policies advanced by Administration spokesmen at the July 9, 1981 hearing included invoking the "reciprocity" citizenship provisions of the Mineral Lands Leasing Act (MLLA).

The MLLA provides a leasing system for the development of specified mineral resources located on Federal onshore lands.[71] United States citizens, associations of such citizens, and corporations organized under U.S. or state law are permitted to hold such leases.[72] The statute prohibits stock ownership by aliens in companies holding Federal leases if their countries impose certain investment restrictions on U.S. citizens:

> Citizens of another country, the laws, customs, or regulations of which deny similar or like privileges to citizens or corporations of this country, shall not by stock ownership, stock holding, or stock control, own any interest in any lease acquired under the provisions of this (Act).[73]

If it were determined by the Secretary of the Interior that the laws or customs of another country, such as Canada, do not treat U.S. citizens the same as Canadians, then Canadians would be prohibited from owning any stock interest in any MLLA lease. Under the terms of the Act, the government would move to cancel leases, cause them to be forfeited or require the interest in the lease to be sold.[74] The plain language of the Act as well as its legislative history—which will be examined in detail below—make it clear that the purpose of the reciprocity provision was to afford American companies access to minerals in foreign countries on the same terms they are afforded such access in the United States. Retaliation for failure to afford equal treatment is not only contemplated, but commanded.

According to the July 9, 1981 testimony of Treasury Under Secretary Sprinkel, the Administration had asked the Department of the Interior to expedite its review of whether or not Canada met the reciprocity test of the MLLA.[75] However, the review was not com-

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[71] 30 U.S.C. § 181 of et seq. (1979) The act's provisions cover coal, phosphate, sodium, potassium, oil, oil shale, native asphalt solid and bisolid bitumen, bituminous rock, and gas.

[72] 30 U.S.C. § 181.

[73] Id.

[74] 30 U.S.C. § 181(h). The U.S. Supreme Court has also held that the Secretary of Interior can administratively cancel a noncompetitive oil and gas lease if it is not known to contain valuable oil and gas deposits, and after notice to the leasee, the leasee does not correct the defect. *Boesche* v. *Udall*, 373 U.S.C. 472 (1963).

[75] Hearings, p. 278.

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pleted until 7 months later, when on February 2, 1982, the Secretary determined Canada was a reciprocal country.[76] The events leading to this decision are a monument to Department of the Interior footdragging. Furthermore, the logic of the Associate Solicitor's Opinion Memo and the Secretarial Decision Paper justifying a finding of reciprocity is tortured, unpersuasive and inconsistent with the purposes of the legislation. Secretary Watt, as the administering official, failed in his sworn duty to uphold the law. Finally, as described in chapter III, U.S. companies have recently been the targets of unfair tender offers by Canadian companies. These usually occur and are completed in a very brief time period. Thus, to the extent that enforcement of the MLLA against Canada was considered to be part of a strategy to influence Ottawa and protect U.S. corporations from raids, any prospects for success were lost by Secretary Watt's footdragging.

A more complete description of that footdragging is detailed in a separate report on the Contempt of Congress proceedings against Secretary Watt. Because of his refusal to work with the Subcommittee on Oversight and Investigations, a subpoena was issued and ultimately the Committee on Energy and Commerce cited the Secretary for contempt. Before the matter was brought to the Floor of the House of Representatives for further proceedings, the White House made all the necessary documents available for inspection and further contempt proceedings were thus obviated.

The process of making reciprocity determinations.—Prior to the procedure instituted in late 1981 by Secretary Watt, reciprocity decisions under the MLLA had been made in an ad hoc manner. As described by the Acting Assistant Solicitor:

> Determinations of foreign reciprocity under 30 U.S.C. Section 181 have never been governed by regulations or other formal procedures—In the distant past, reciprocity was considered on a case-by-case basis with set procedure.[77]

In recent years a system evolved by which the Department maintained a list of "reciprocal countries". Countries whose names did not appear on the list were considered "nonreciprocal". Interior's Bureau of Land Management (BLM) created the list by obtaining from the appropriate U.S. Embassy summaries of the mineral laws of the country in question and the recommendation on the question of reciprocity.* The quality of the reviews varied, in part because the Department of the Interior gave little guidance to the Department of State regarding factors to consider in making a finding of reciprocity. Generally, the determinations were perfunctory. At one time, for example, the American Embassy asked an official from the Canadian Department of Energy, Mines and Resources whether his country qualified for reciprocal status. Not surprisingly, the official responded in the affirmative. There appeared to be no independent effort by State or Interior to check the accuracy of this assertion.[78]

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[76] The Secretarial decision paper and the Associate Solicitors opinion memorandum are printed as app. A.

[77] Letter from Donald P. Truesdell, Department of Interior, to Franklin Willis, Feb. 29, 1980, and from Theodore W. Kassinger to Dale C. Zimmerman, Aug. 22, 1980.

[78] See telegram from U.S. Embassy, Ottawa, to the Secretary of State, Washington, D.C., Feb. 17, 1977.

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Secretary Watt's review of the Canadian reciprocity question was unnecessarily lengthy and overcomplicated

When the Secretary testified before the Subcommittee on August 6th, 1981, he announced the initiation at that point of a formal fact-finding effort designed to make determinations with respect to Canada. He described the process as follows:

> The purposes of this effort are to protect the rights of all interested parties to due process under the law and to arrive at the decision that is in the best interests of the U.S.
>
> The fact-finding effort will involve the following steps: First, I will make a formal request that the heads of all relevant Federal agencies give me their opinions on what standard should be applied in making reciprocity decisions, whether Canada is a reciprocal nation under these standards, and, if Canada is not a reciprocal nation, what steps should I take in applying the Mineral Lands Leasing Act.
>
> Second, I will review these recommendations and decide whether there is sufficient evidence that Canada is not reciprocal to proceed with our review.
>
> If such evidence exists, I will publish a notice in the Federal Register requesting public comments. Upon the closing of the public comment period, I will make a preliminary determination as to Canada's reciprocal status.
>
> Finally, after review of all relevant evidence, I will decide whether Canada is a reciprocal nation, and, if it is not reciprocal, what sanctions should be applied.[79]

The Secretary promised "speedy and vigorous" action in making the determination, but as subsequent events show, this procedure appears to have been adopted primarily as a tactic to delay the determination with respect to Canada and perhaps other countries and to divert Congressional attention.

Before discussing the results and the rationale of the decision, it is useful to review the sequence of events.

December 1980.—Staff of the Department of Interior, Bureau of Land Management, on its own initiative, begin a low priority review of the reciprocity list. Information is sought from the Department of State to assist in the review.

January 1981.—The New Mexico Office of the Bureau of Land Management informs Washington that it is inclined to deny a lease sought by Canadians on the grounds that Canada does not grant U.S. citizens "similar or like privileges" in accordance with the MLLA.

March 1981.—Washington directs the New Mexico State Office to consider Canada reciprocal pending outcome of the review of reciprocal countries then underway.

March 26, 1981.—St. Joe Minerals files a petition with the Department of Interior requesting that Canada be declared a nonreciprocal country.

April 21, 1981.—The Department of the Interior determines it is not required to act on St. Joe's petition. It is "outside the adjudicative process and not subject to any formal regulatory procedure".

May 7, 1981.—The Department of the Interior testifies before a Congressional Subcommittee regarding pending legislation imposing sweeping prohibitions on foreign investment in leases on Federal lands. The Department of the Interior promises "to review the manner in which the Department has implemented the reciprocity provision . . . and . . . whether Canada is a reciprocal nation within the meaning of the Mineral Lands Leasing Act".[79a]

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[79] Hearings, p. 356.

[79a] The "Secretarial decision" paper released to the press in February 1982 begins as follows: "In August 1981 the Department began a review . . ."

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July 6, 1981.—Chairman Dingell and Chairman Wirth write to Secretary Watt asking eight questions regarding implementation of the Mineral Lands Leasing Act for use in conjunction with a mark-up on pending legislation.

July 7, 1981.—Conoco files a petition with the Department of the Interior requesting immediate review of Canada's status.

July 9, 1981.—Administration spokesmen testify at Oversight Subcommittee hearing that the Department of the Interior has been asked to "expedite its review of Canada's reciprocal country" status.

July 14, 1981.—Bureau of Land Management staff write a memo making preliminary recommendations regarding Canadian status.

July 17, 1981.—Scheduled appearance by Secretary Watt to testify before the Subcommittee on Oversight and Investigations regarding the MLLA. Secretary Watt requests postponement of hearing to prepare for trip to Canada.

July 22, 1981.—Rescheduled date for appearance by Secretary Watt before the Subcommittee on Oversight and Investigations. Hearing cancelled when legislative liaison leaves message at Subcommittee offices on July 21 that Watt "has been called to a cabinet meeting." Telephone calls from both the Chairman and the Subcommittee staff seeking to reschedule the hearing go unreturned.

August 6, 1981.—At Oversight and Investigations hearing Secretary Watt announces new decisionmaking procedure for reciprocity determinations. He reports ready to proceed with decision on Canada, and it will require 90 to 120 days to complete the process. He commits to "speedy and vigorous" action on the issue.

August 7, 1981.—Interior seeks comments from nine departments and agencies as to what standards the Department should follow in making the reciprocity determination and their views on whether or not Canada is a reciprocal country.

August 12, 1981.—Interior seeks comments from the Justice Department on the appropriate procedures for determinations under the Mineral Lands Leasing Act.

September 28, 1981.—Subpoena issued by the Subcommittee on Oversight and Investigations to Secretary of the Interior for documents relevant to determinations of reciprocity. (Served on October 2, 1981).

October 14, 1981.—Hearing at which the Secretary of the Interior refuses to provide subpoenaed documents relevant to determinations of reciprocity. Chairman Dingell notes that no notice seeking public comments on the status of Canada in accordance with the procedure outlined on August 6th has been published.

October 22, 1981.—Assistant Secretary of the Interior testifies before a House Government Operations Subcommittee that the Department is developing a procedure for implementing the reciprocity provisions of the Act. He predicts it will be in place at the end of the year.

November 6, 1981.—Subcommittee issues public notice of hearing on the refusal of the Secretary to submit subpoenaed documents. Department of the Interior sends notice seeking comments on the status of Canada to the *Federal Register*. (Published on November 12, 1981).

November 13 and 19, 1981.—Subcommittee hearings on the refusal to submit subpoenaed documents.

February 1, 1982.—Subcommittee Members notified of vote on question of contempt for failure to provide subpoenaed documents.

February 2, 1982.—Secretary of the Interior makes decision on reciprocity status of Canada.

As is obvious from the chronology, Secretary Watt's novel two-step determination process was little more than a deliberate delaying technique. When announced, the review of Canada's reciprocity had been underway for at least eight months. The solicitation of views from the nine agencies was also unnecessary. Three of those agencies had in public testimony before the Subcommittee a month earlier expressed their views that Canadian policies discriminated against American investors. Only four other agencies responded, including the Justice Department, which commented on the legal interpretation of the Act. The SEC made no comment on the issue. The agency responses were generally prompt, yet it was not until three months later that the Department, on the day of the announcement of a Subcommittee hearing, issued a notice seeking public comment. In addition to the public hearing record, which should have provided "sufficient evidence that Canada is not reciprocal to proceed with our review", there was substantial other information to establish probable cause justifying the review. For example, within the Department, it was the staff's view that there was adequate information to conduct a review of Canada. A July "draft" Solicitor's memorandum stated that "we have collected from various sources nearly all the factual information necessary to make a determination on Canada".[80] In addition, the Canadian Foreign Investment Review Agency regularly published information regarding denied applications and its policy was to deny applications by foreign companies in the energy sector.

Finally, after three months of review of other agency comments,[81] the Department published a notice seeking public comment on November 12, 1981. The perfunctory notice, short, general, and devoid of any analysis of the question based on the consultations with the other agencies, could have been published much earlier. The ultimate determination regarding Canadian reciprocity was finally made more than a year after the Subcommittee initiated its investigation, nine months after assurances to a Congressional Committee that the review was underway, and six months after the Oversight had been promised "speedy and vigorous action". It may be more than coincidence that the finding on Canada was made the day after the Oversight Subcommittee scheduled a meeting to determine why Secretary Watt should not be held in contempt for failing to provide MLLA information subpoenaed by the Subcommittee.

As illustrated in the following colloquy at the August 6th hearing,[82] Secretary Watt went to great lengths to avoid committing himself to a timetable of action:

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[80] Undated memorandum from Solicitor to Under Secretary, U.S. Department of the Interior, "Legal issues in Representative Dingell's letter of July 6 on Canadian reciprocity," at p. 5.

[81] 46 Federal Register 55786.

[82] Hearings, p. 361.

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Mr. WALGREN. How long will it take to get through the process that you outlined in your testimony before we come to the point where there would be a binding finding?

Secretary WATT. I think that will depend upon the factual situation, of course, and how much public participation there is and how much briefing would be done.

But I do not anticipate that it could be done in less than 90 to 120 days, if you honor due process requirements.

Mr. WALGREN. Can it be done within 120 days?

Secretary WATT. Possibly, but probably not within 90 days. I mean, that is an area, I am giving a range for that purpose.

Mr. WALGREN. What would delay it beyond 120 days?

Secretary WATT. The need to allow public involvement and the due process to be played out so that you could hear from the affected parties.

Mr. WALGREN. Can you make a firm time estimate of when we can have this finding? It seems to have gone on for some time from the committee's first inquiry, and we still are only at the point of starting the process.

Secretary WATT. We are just starting the process, and so it is the time from here into the future. And I am not prepared to give you an exact date.

Mr. WALGREN. What is the degree of your commitment to move as directly as possible on this?

Secretary WATT. We are commencing now.

Mr. WALGREN. But the Committee's problem, or my problem from just reading the record, is that the first inquiries on this questions were made a number of months ago, and the only thing that is being presented today is that you have asked the Federal agencies to look at this problem.

It seems to me that the public has a right to expect, particularly when there is a law that is involved that may or may not be properly enforced, a specific timetable from the Administration.

Secretary WATT. We will go rapidly as due process will allow. And the first effort, of course, was that which was needed to establish historical basis for this, to see how it had been handled in the past, what the previous Administrations had done about these subject matters, and how we would move from the past into the present, into the future.

Selective concerns about due process.—Secretary Watt expressed grave concern about due process with respect to the Canadian decision. However, those same concerns were not carried over to the reciprocity determinations of other countries, particularly Kuwait.

The Secretary described his feelings about due process with respect to Canada in a colloquy with Congressman Wyden, who sought to determine the need for the two-stage decision procedure:

Secretary WATT. The question you present is an understandable one. And it is one of the frustrations in the judicial and quasi-judicial areas, because while some people may feel that there are sufficient indicators to make such a finding, the due process that we guarantee in this country requires that you not prematurely make that judgment until you have allowed the parties to come forward.

So it would be improper for me to answer that question as well.

Mr. WYDEN. Could you list for me the specific factual determinations that you still have to make? What are those?

Secretary WATT. I am not in a position to do that, and I am not prepared to do that.[83]

Throughout the testimony, the Secretary also conveyed what appeared to be a more generalized concern about establishing general procedures to deal with questions of reciprocity. He stated at one point:

Department regulations require there be an establishment procedure for handling this type of problem. Once that procedure then is established which we are telling you about today, then we will address the Canadian situation. That need not be a dilatory manner. The procedure can be set up very quickly. In fact, we have it set up so that we are now ready to proceed on the Canadian issue.

Mr. DINGELL. Would you submit to us those regulations, Mr. Secretary?

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[83] Id., p. 363.

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Secretary WATT. Yes we would.

Mr. DINGELL. Also any information you may give us, including the language of rules and regulations relative to the process [the information requested was not available to the subcommittee at the time of printing (of hearings)].[84]

These regulations were never submitted to, or identified for, the Subcommittee (see also hearing record serial number 97-89, which includes the submissions of the Department in response to questions posed at the August 6th hearing).

Chairman Dingell's questioning of Secretary Watt regarding the manner in which due process could and would be afforded reflects the Subcommittee's frustration in understanding why the new procedure was necessary. Chairman Dingell felt that the existing procedures were adequate to assure due process; Secretary Watt persistently argued that new procedures were required.

Mr. DINGELL. * * * Mr. Secretary, there is no requirement for due process in connection with the finding of reciprocity, is there? You can just proceed through the orderly hearing process inside the Department.

Secretary WATT. I would assume that any decision would be contested through the courts in an aggressive manner. And I think due process is a requirement.

Mr. DINGELL. But, Mr. Secretary, the due process comes in connection with the individual, once the determination has been made and enforcement such as cancellation, forced disposition of leases takes place, that is where the individual due process occurs.

Due process is found under the actions which is taken by the Department in connection with its initial rulemaking action by complying fully with the procedures of APA, am I not correct?

Secretary WATT. If I am following you correctly, that may be right.

* * * * * * *

Secretary WATT. But it is important that you know where you are going to come out in the way of enforcement techniques and alternatives that are in the U.S. interests, rather than——

Mr. DINGELL. The first step is the question of reciprocity. You have got to make that ascertainment.

Then, the individual question of due process arises in connection with your enforcement actions based on your findings of reciprocity. Now, is that not so?

Secretary WATT. It would seem to me that you need, to make the decision on reciprocity, that you need to allow proper input to make that decision. Now——

Mr. DINGELL. Mr. Secretary, you achieve that through complying with the provisions of APA in terms of your procedural steps toward the determination of reciprocity or nonreciprocity.

Secretary WATT. OK. The procedures need to be established for determining reciprocity.

Mr. DINGELL. Those are already defined in the Administrative Procedures Act.

* * * * * * *

So the point I am making is you simply follow APA in arriving at your determination as regards reciprocity. I am saying you have no need to generate any special processes or procedures inside the Department for making, for moving toward a finding of reciprocity or nonreciprocity.

Secretary WATT. It seems to me that we would follow APA to establish the regulations or rules under which we would proceed to determine reciprocity.

Mr. DINGELL. No, no, no. You simply, you have the option as I read it, Mr. Secretary, of simply going out and finding reciprocity, either on a case-by-case basis, or the basis of establishing some kind of general rule.

I would think if you go out to establish some kind of a general rule, you could probably take the decision on reciprocity or nonreciprocity clear through the end of this administration and the succeeding administration. I don't think the national interest tolerates that kind of delay.

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[84] Id., p. 381.

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Now, I would call to your attention, Mr. Secretary, that in the past, decisions as regard to reciprocity have been made without any rulemaking procedure. It has been done simply on the basis of a finding.

This action has never been challenged in the courts, to the best of my knowledge, on the basis of any denial of due process. So the point I am making is that historically and on the basis of precedence, you have full capacity to go out and make the necessary findings without this long and tedious process that I gather you are contemplating.

Secretary WATT. It can be described as long and tedious. And we feel that under the regulations controlling the Department of Interior, there is a requirement that you set up the procedure that we are following to pursue it. * * *[85]

The Justice Department agreed with the Chairman's view that extensive procedures were not necessary. An Assistant Attorney General and members of the Justice Department staff advised Under Secretary of the Interior Hodel that "actions under the reciprocity provision of the MLLA are not subject to the Administrative Procedure Act".[86] It was only necessary that the Secretary not act "arbitrarily or capriciously" and that "a suitable factual basis must be established for his decision".[87]

In the face of all evidence and reasoned opinion to the contrary, the Department continued to assert it needed elaborate procedures. At a Congressional hearing three months later, in which questions were raised concerning Kuwait, the Departmental procedural concerns were raised again, but this time the application of the procedures took a strange twist. On October 22, 1981, the Assistant Secretary for Policy, Budget and Administration stated in prepared testimony "We are now seeking to develop a predictable mechanism which clarifies the procedures for both stages, determination and implementation".[88] He testified that the Department had to make a determination regarding the procedures to be followed and that the procedures would be in place by the end of the year. Then he said that countries whose names did not appear on the reciprocal list might be reciprocal, and that leases could be issued pending a determination for each country.[89] This reversed longstanding Departmental policy, appeared to conflict with the MLLA, and disregarded totally the "due process" concerns described at the August 1981 hearing by secretary Watt. Thus, the anomalous situation arose whereby the process being religiously pursued to make reciprocity determinations with respect to Canada was not applied to Kuwait, a country whose officials had previously understood that the country could not be considered reciprocal unless it had been placed on the list. Moreover, to suggest that countries with nationalized mineral resources, such as Kuwait, do not by definition violate the reciprocity test is absurd. Specifically, in August 1980, a State Department cable indicated that an official of the Kuwait government had been "informed that there is a U.S. legal requirement that foreign buyers must be on an approved Department of the Interior list before they can buy into American companies."[90]

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[85] Id., pp. 365-366.

[86] Letter from Donald Paul Hodel, Under Secretary of the Interior, to William P. Baxter, Assistant Attorney General, Department of Justice, Aug. 12, 1981.

[87] Id.

[88] Statement of Assistant Secretary West before the Subcommittee on Commerce, Consumer and Monetary Affairs of the Committee on Government Operations, Oct. 22, 1981, p. 5.

[89] See transcript, pp. 94-95.

[90] Telegram from U.S. Embassy, Kuwait, to the Secretary of State, Washington, D.C., Aug. 21, 1980. The cable has been declassified.

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Accordingly, the Department of State urged a determination by the Department of the Interior with respect to Kuwait. But, under the new timetable laid out by Assistant Secretary West, the determination was not to be made until December 1981 at the earliest. One effect of this delay was to turn a blind eye to the ultimately successful effort by the Kuwait National Petroleum Corporation to acquire Santa Fe International, an American energy company with extensive mineral leases on Federal lands.

The due process argument seems to have been litte more than an excuse to delay the Canadian decision. Had the Subcommittee not held Secretary Watt in contempt of Congress for failure to submit subpoenaed materials, and pursued the matter through the full committee, there is no telling how long the Secretary would have delayed. The Chairman's prediction that the "development of procedures" would delay the matter through the "end of this Administration"[91] might well have come true. This surmise is consistent with the discovery, upon review of the subpoenaed documents, that high level officials from the Interior Departmen. appeared to have made up their minds well in advance of the actual decision. The conclusion becomes inescapable—based upon review of State Department cables concerning Kuwait—that Secretary Watt strongly favors the maximum development of U.S. resources by foreigners whether their countries grant reciprocity or not. As reported in The Washington Post on May 15, 1981 the State Department in Washington cabled the U.S. Embassy in Kuwait that:

> Interior staff discussed the issue with Secretary Watt, who proved very sympathetic both to an affirmative determination for Kuwait and the general idea of promoting investment in firms developing U.S. mineral resources.[92]

Moreover, in conversations with Senior Kuwaiti officials, Treasury Secretary Regan, who was visiting the area, was authorized to say that:

> Secretary Watt has been consulted and is sympathetic to the Kuwaiti request, and indeed supports increased levels of investment (including foreign) in U.S. corporations developing U.S. mineral resources.[93]

The cable also noted that because of the lack of legal standards and the specter of lawsuits challenging Interior's determination, the department had concluded that it could not announce an affirmative determination "at this time". However, the cable added that:

> Interior has embarked on a review attempting to rationalize the practice under the act by which affirmative determinations for such countries are made. [emphasis supplied][94]

An Interior Department spokesman publicly revealed the Administration's sentiment in testimony before another House subcommittee on October 22, 1981. J. Robinson West, assistant Secretary for Policy, Budget and Administration, said that the Reagan Administration was favorably inclined to grant leasing privileges on Federal lands to the Kuwait National Petroleum Company even

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[91] Hearings, p. 366.
[92] Washington Post, Nov. 6, 1981, quoting from a telegram from Secretary of State to the U.S. Embassy, Kuwait, May 15, 1981.
[93] Id.
[94] Id.

though Kuwait was not on the list of nations that have been found to comply with the reciprocity provisions of the MLLA.[95]

Since the Secretary had obviously prejudged the issue, it came as no surprise that Canada was found to be a reciprocal nation in early 1982.[96] Notwithstanding his promise that he intended to "apply the law in accordance with its terms,"[97] Secretary Watt clearly demonstrated his reluctance to do so. Moreover, he deceived the Congress and made a mockery of the Department's decisional process.

The most recent MLLA action by the Department of the Interior further illustrates the spurious nature of Secretary Watt's due process claim. Despite the elaborate decisional procedure established in the Canadian case, the Department has now returned to a less formal process. According to a June 25, 1982 Federal Register notice,[98] there will no longer be a list of reciprocal countries. Rather, a list of non-reciprocal countries will be prepared. Countries not on the list will be considered reciprocal. The Department also reserved the right to review informally whether or not specific countries grant similar or like privileges to U.S. citizens and to issue determinations without requesting public comments. This total reversal of recent practice appears designed to maximize the investment in U.S. mineral resources by foreign interests while allowing the Department of the Interior to resume its usual bureaucratic lethargy.

B. The Decision with Respect to Canada.—On February 2, 1982, Secretary Watt determined that Canada was a reciprocal country. That decision was based in large part on an advisory memorandum from the Interior Department's Associate Solicitor.[99] The memo recommended that the legislative history of the Act be interpreted to the extent possible to assure that application "of a statutory provision should be reasonable calculated to accomplish Congressional purposes". According to the Associate Solicitor, the legislative history of the MLLA was that the "reciprocity provision should, to the extent possible, be applied to prohibit the uncontrolled and unchecked exportation of domestic mineral resources and to discourage foreign retalitation against investment by the U.S. interest." There, the historical analysis stopped.

The Associate Solicitor's analysis of the legislative history is an example of that maxim of statutory construction, "Látorúm de ménte nihíl tuae faveat nisi cáusae", or, "If pertinent legislative history doesn't support your case, ignore it". His memo glosses over a key portion of the legislative history which dealt with the MLLA's intended use for retaliatory purposes. The Associate Solicitor made passing reference to the fact that the House debate included a discussion, among other matters, of the use of reciprocity "* * * to retaliate against foreign governments."

While debating the Act, Members of Congress clearly expressed their concern that national security interests required that U.S. citizens control domestic mineral resources.[100] Some Members fa-

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[95] New York times, Oct. 23, 1981.
[96] See app. A for Secretarial decision paper.
[97] Hearings, p. 356.
[98] 47 FR 27623, June 25, 1982.
[99] This memo is printed as app. A.
[100] 58 Congressional Record 4054 (1919).

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vored an absolute prohibition on foreign ownership or control over mineral leases on public lands.[101] Others were concerned that such a prohibition on foreign ownership in the United States could lead to retaliatory action by foreign governments with the result that U.S. citizens would lose their mineral holdings in foreign countries.[102] The Senate originally proposed prohibiting foreign ownership, then adopted language allowing alien ownership of leases through stock, provided that the government could take over and operate the leases and could require the sale of mineral products in this country. That language was ultimately rejected in favor of the House amendment:

> Citizens of another country, the law, customs or regulations of which deny similar or like privileges to citizens, or corporations of this country, shall not by stock ownership, stock holding or stock control, own any interest in any lease acquired under the provisions of this chapter.[103]

When the House Committee recommended the amendment of the language, it stated that it specifically sought to avoid retaliatory actions from foreign governments which might result from the proposed prohibition on foreign ownership:

> The main argument for the Senate draft was that foreign control of domestic corporations operating a lease under the Act would result in large exportations of oil, coal and other minerals covered by the Act, and thereby deplete the domestic supply. Under the House reciprocal clause above mentioned, it is obvious that the citizens of the United States could largely offset such a result by their own operations in foreign countries, or, if an acute situation every developed, a general embargo against exportation would be a sufficient remedy.[104]

The purpose of providing a retaliatory tool was discussed in some detail in the floor debate. That debate, which the Associate Solicitor failed to discuss in his memorandum, is as follows:

> Mr. EVANS. of Nebraska. What is the object of restricting persons who may be members of corporations in the latter part of section 1, in the last proviso?
>
> Mr. SINNOTT. Some foreign countries discriminate against citizens of the United States in stock ownership.
>
> Mr. EVANS of Nebraska. Then why is it not the money of the alien as good as the money of the citizen?
>
> Mr. SINNOTT. We think our own citizens are entitled first to the development of the oil fields.
>
> Mr. EVANS of Nebraska. Why not strike out the provision that permits any alien to become interested?
>
> Mr. SINNOTT. Because those who discriminate against us, if we retaliate, perhaps they may do away with the discrimination.[105]

And at another point:

> Mr. SNELL. I move to strike out the last two words, for the purpose of asking a question of the chairman of the committee. Under the provisions of this bill——
>
> Citizens of another country the law, customs, or regulations of which deny similar or like privileges to citizens or corporations of this country, shall not by stock ownership, stock holding, or stock control, own any interest in any lease acquired under the provisions of this act.
>
> As I understand it, the British Government does not allow any alien to own any oil lands under the control of that Government. According to this act, what would

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[101] Id.

[102] Id., 4112-13 and 4166.

[103] Id., 737 (1920).

[104] House Committee on the Public Lands, Mining of Coal, Phosphate, Oil, etc. Report to accompany S. 2775, H.R. No. 398, 66th Congress, at 11. (1919).

[105] 59 Congressional Record 7529 (1919).

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be the result if a British subject owned stock in any one of our oil companies? What would be the situation in which he would find himself?

Mr. SINNOTT. If the British Government discriminates against us, we meet the discrimination by denying to its citizens the rights that are withheld from us.

Mr. SNELL. If I were a British subject and held some stock in one of these oil companies, would I be forced to sell it?

Mr. SINNOTT. The stock could be declared forfeited, under the forfeiture clause in the bill.

Mr. SNELL. There is no protection then for any foreigner who happens to own stock in one of our oil companies, is there?

Mr. SINNOTT. Not if his Government denies us the same rights.

Mr. SNELL. I understand the British Government forbids aliens to own or control any of their oil lands.

Mr. SINNOTT. That representation has been made to the committee, and to individual members of the committee.

Mr. SNELL. Does the gentleman know whether it is true or not?

Mr. SINNOTT. I have no reason to doubt the representation.

Mr. SNELL. Then a British subject would be obliged to forfeit or sell his stock, and get out of the country as quickly as possible.

Mr. SINNOTT. That would be the interpretation I would place upon the law.[105a]

The Associate Solicitor dealt with this entire discussion of the precise language included ultimately in the statute by stating:

> The House debate focused upon * * * the use of reciprocity to retaliate against foreign governments which discriminate against United States interests * * *[106]

Glossing over, and then excluding the House debate regarding the reciprocity considerations from his summary of the legislative purpose appears deliberate. The Solicitor was fully cognizant of the provisions. Indeed, in a memo prepared earlier in the summer,[107] he responded to the question, "Does the Act contemplate retaliation against citizens of nonreciprocal countries?" by saying "Yes, but only within the Act's limits". Furthermore, at the August 6th hearing, Chairman Dingell made a point of reading the relevant legislative history into the Record and admonishing "Mr. Secretary: I think the legislative history of this is really much more clear than the Administration would have us believe".[108]

The Associate Solicitor then summarized previous Departmental interpretations of the Act, all of which have generally construed it so as to find a country reciprocal. These interpretations include the following: The fundamental question regarding like or similar privileges is determined according to whether or not Americans can own a stock interest in foreign corporations; a country whose energy resources are nationalized is not considered a "nonreciprocal country"; and with respect to those resources, a country can be considered partially reciprocal up to certain percentage of ownership (for example, if the country allows foreigners to own 20 percent of the stock in corporations, then it is considered to be 20 percent reciprocal.*)

He followed that summary with a description of the manner in which reciprocity determinations should be made: first, a determination must be made whether or not U.S. citizens can own stock in the country's corporations, and, if so, then the country is presumed reciprocal unless there are regulations regarding that ownerships which are "unduly restrictive"; second, even if the country allows

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[105a] 59 Congressional Record 7528 (1919).
[106] See app. A.
[107] Supra, note 80 at p. 2.
[108] Hearings, p. 369.

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stock participation by U.S. interest, it can be considered nonreciprocal if it restricts participation in the country's mineral resources on public lands; and third, even if there are certain restrictions on stock participation, if it cannot be determined to a certainty the percentage of stock ownership, it is "preferable to avoid speculation and conjecture and refrain from attempting to mirror the percentage ownership".

Most of the Solicitor's analysis is consistent with the previous interpretations of the Act. But his requirement that "mirroring" may be applied only when the Secretary can determine "with precision" the extent to which a foreign country is reciprocal, is a new wrinkle assuring that the Act will not apply to the Canadian situation. Furthermore, it is inconsistent with the language and purposes of the Act.

A secretarial Decision Paper which, according to the Department, formed the basis of the decision, relied in large part on the Solicitor's Opinion. It recommended that Canada be found reciprocal, stating "The Department's review indicates the Canadian laws, customs and regulations do not deny U.S. citizens or corporations the privilege of acquiring an interest in the mineral resources of Canada".

Foreign Investment Review Act.—The Secretarial Decision Paper [109] examined the practices of the Foreign Investment Review Agency, the Canadian Government body that must approve foreign investment in Canada. Notwithstanding the restrictive practices of that body, which are especially pronounced in the energy area, the Department found Canada to be a reciprocal country. The reasoning was as follows:

There is no general rule of the FIRA which prohibits investment by U.S. citizens through stock holdings in oil and gas resources, and

Even though the Agency "on occasion refused to permit American corporations to acquire Canadian corporations which appeared to have interests in Canadian oil and gas resources", the Department concluded that it is "neither the custom nor the practice of the Agency to deny U.S. citizens the privilege of acquiring an interest in Canada's oil and gas reserves" since such applications were not disapproved most of the time.

Technically, the Department is correct, as there is no absolute prohibition against such an investment. But, with respect to prohibitions on investment, FIRA's policy at that time was a flat prohibition against the purchase by or transfer between U.S. companies of Canadian energy assets. In addition, the Department used the wrong statistics to discuss the question of applicability to mineral resources. Instead of review all specific instances where FIRA reviewed energy and mineral applications, Interior relied on aggregate data, which included all types of applications. The use of the wrong figures, which served to buttress the Department's case, was not accidental. Last summer, the Solicitor expressed the view that FIRA seemed to have had an adverse effect on U.S. investments in Canadian mineral resources, noting that the number of U.S. appli-

[109] See app. A.

cations to "acquire mineral related acquirees" had dropped by more than one-third in the one-year period.

The Secretarial Decision paper states:

> The requirement of COGA (Canada Oil and Gas Act) which mandates that corporations acquiring production licenses have a Canadian ownership rate of 50 percent or more, does not deny American citizens or corporations the privileges accorded Canadian citizens under the Mineral Lands Leasing Act. Nevertheless, it is clear that the Canadian ownership requirement is discriminatory towards United States citizens and corporations, but it is so in a manner that does not affect the factual determinations the Department must make concerning the reciprocity status of Canada within the meaning of the MLLA.

The Secretarial paper acknowledges that American investors were affected adversely by the lack of equal opportunity for economic return, but, it steadfastly declined to find that Canadian investment policies discriminated against American citizens. The paper reasons that because the fundamental privilege of acquiring interests in stocks is unaffected, Canada is reciprocal within the meaning of the Mineral Lands Leasing Act. The Committee disagrees with that conclusion.

Inadequacies of BLM recordkeeping.—Even if the Secretary had made a decision finding Canada a nonreciprocal country, the Department of Interior would have difficulties enforcing the Act. Moreover, the Secretary had indicated an unwillingness to attempt to overcome these problems. Disclosures of foreign ownership must be made in conjunction with an application for a lease.[110] However, Secretary Watt testified that the Department did not keep information regarding the ownership of leases beyond the first named leaseholder,[111] and that he did not think it would be worth taxpayers' dollars to keep the information up-to-date.[112] "I think it would be bad public policy to set up the computer mechanism to acquire that on a continuing basis." [113] In response to the question: "Do we have the information available to be able to sort out the Canadian investment out of all the other investments in the leaseholds?"[114] Secretary Watt responded that the necessary data could be obtained from other Federal agencies, including the SEC and the Department of Commerce.[115] However, the Department had made no effort to obtain relevant information from the Securities and Exchange Commission.[116]

Under the BLM record keeping-system examined during the course of the August 1981 hearing, information regarding alien ownership is, in fact, not easily retrievable. Qualification statements filed for each lease contain information related primarily to questions of a corporation's authority to act. A stockholder owning

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[110] 43 C.F.R. subpart 3502 (1980).
[111] Hearings, p. 368.
[112] Id., p. 369
[113] Id., p. 373.
[114] Id., p. 368.
[115] Id.
[116] Letter from Matthew Schneider, Director of Legislative Affairs, Securities and Exchange Commission to John D. Dingell, Chairman, Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, Sept. 17, 1981.
The Securities and Exchange Commission is the most obvious and commonly identified of such agencies. However, the ease with which ownership can be traced tends to be overstated. Currently disclosure forms must be filed by the beneficial owers of 5 percent or more of the stock of a company—thus, only the owners of blocks of stocks are easily identifiable. Further, many shares are held in a "street" name, rather than the name of the owner.

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or controlling more than 10 percent of the company is required to provide information regarding his citizenship.[117] Once a qualification statement is filed, subsequent lease applications are filed by referring to the serial number on the original qualification statement, if the qualification statement on file is up-to-date. However, in recent years, no attempt has been made to verify the accuracy of qualification statements nor has a corporate lessee amended its qualification statement to reflect acquisition of stock by foreign investors.[118]

Qualification statements are filed in the BLM's various state offices. The information is not centrally available, nor apparently available in the Washington office.[119] But, the development of a perfect record-keeping system is not a necessary prerequisite to the enforcement of the Act's provisions.

There are sources of information which would bring a potential violation to the attention of the Department. In 1976, the Assistant Solicitor for the Branch of Minerals, the Division of Energy and Resources had made it clear that if reliable information came to the attention of the Department that ownership had fallen into ineligible hands, "the Department would have the statutory duty to investigate and, if the evidence was adequate, to initiate appropriate legal actions."[120] The Secretary himself stated that obtaining assistance from other Federal agencies would be appropriate. Transactions such as the tender offers for larger companies are frequently reported in the newspaper—thus, a tender for a company known or suspected to hold leases on Federal lands would provide the opportunity to inquire into the matter of whether or not ineligible aliens hold stock in that company. Of course, the result of a system that does not track adequately ownership will be that ineligible alien stockholders will go unidentified. But, many other Federal agencies are not paralyzed into inaction just because all the possible information is not easily at their fingertips.

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[117] 43 C.F.R. § 3502.4-1 (1980).

[118] Unpublished paper, Jerry M. Brady, Alien Ownership of Oil and Gas Leases under the Mineral Lands Leasing Act, Apr. 12, 1981, at 6 and 7.

[119] Supra, note 117, and conversation with John Campbell, Department of the Interior. Sept. 4, 1981.

[120] Letter from J. Edmund Rast to Frederick N. Ferguson, Assistant Solicitor for Branch of Minerals, Feb. 23, 1976, and Ferguson to Rast, Mar. 1, 1976.

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APPENDIX A

U.S. DEPARTMENT OF THE INTERIOR,
OFFICE OF THE SOLICITOR,
Washington, D.C., February 2, 1982.

Memorandum to Secretary.
From Associate Solicitor, Energy and Resources.
Subject Determinations of Reciprocity under Section 1 of the Mineral Lands Leasing Act of 1920 (30 U.S.C. § 181).

We have been requested to advise you on several issues concerning the so-called "reciprocity" provision of section 1 of the Mineral Lands Leasing Act of 1920, 30 U.S.C. § 181.[1] We understand the primary reason for your request is to insure that the appropriate procedures are used and the appropriate legal standard is applied in determining Canada's reciprocity. Accordingly, this opinion does not address the many issues relating to the application of the reciprocity provision, but rather addresses only questions which have been raised specifically in connection with the decision on Canada's reciprocity.

I. STATUTORY PROVISIONS

Enactment of the Mineral Lands Leasing Act ("Act") in 1920, provided a new direction for the management of certain of the nation's minerals. The Act generally removed certain enumerated minerals from the operation of location and mining laws and established guidelines for leasing such minerals. In so doing, Section 1 of the Act limited leasing of the enumerated minerals and land containing such deposits to citizens of the United States, associations of such citizens, domestic corporations and, in limited situations, municipalities. Citizens of foreign countries may obtain interests in leases on public lands but only through ownership, holding or control of stock in a domestic corporation. (See discussion between Senators King and Lenroot, 58 Cong. Rec. 4167 (August 22, 1919); and Senators Lenroot, Phelan and Pittman, 58 Cong. Rec. 4785 (September 3, 1919).) The acquisition of interests in leases by foreign citizens through stock ownership, holding or control is guided by the following provision:

"Citizens of another country, the laws, customs, or regulations of which deny like or similar privileges to citizens or corporations of this country, shall not by stock ownership, stock holding, or stock control, own any interest in any lease acquired under the provisions of this Act." [30 U.S.C. § 181.]

As is apparent, this statutory language does not provide specific guidance as to the implementation and administration of the provision. Analyses of the legislative history and prior construction are important in determining the proper procedures for making decisions on reciprocity.

II. INTERPRETIVE AIDS

A. Legislative history

While the legislative history is limited, it provides some insight into the Congressional intent when enacting the reciprocity provision. Initially it should be noted that both the Senate and House legislative histories are relevant. The bill, which after a number of modifications was passed by the 66th Congress as S. 2775, initially prohibited any foreign interests in mineral leases. However, the Senate amended the original provision to allow foreign interests "through stock ownership or other-

[1] The reciprocity provision also applies to leases issued under the Mineral Leasing Act for Acquired Lands, 30 U.S.C. § 351 et seq.

*NOTE.—Attachments mentioned in this memorandum are not included.

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wise" if the lease contained a specific clause authorizing the President in his discretion to take the lease over and operate it. 58 Cong. Rec. 4160, 4171 (August 22, 1919). Except for the takeover provision, this clause was virtually identical in its references to lease interests and foreign stock interests to the current reciprocity provision, which was added by the House to S. 2775 and adopted by the Conference Committee in the bill that was enacted. As a result, the Senate debate concerning these interests should be accorded weight equal to the House debate when examining the legislative history of these aspects of the reciprocity provision. While the debate in the House of Representatives and the report of the House Committee on Public Lands (H.R. Rep. No. 398, 66th Cong., 1st Sess. (1919)) on S. 2775 bear directly on a proper interpretation of the reciprocity provision, there was no Senate report on S. 2775 and the Conference Report on S. 2775 provides virtually no assistance in interpreting the reciprocity provision. H.R. Rep. No. 600, 66th Cong., 2d Sess. (1920).

The legislative history generally indicates that Congress had two major concerns with foreign acquisition of mineral leases. First, Congress was concerned that mineral resources on public lands might become dominated by foreign interests. The concern Congress had with such domination seemed to be the unchecked exportation of minerals to foreign countries which discriminate against United States ownership of their minerals. Second, Congress was concerned that the benefits from operation of the public land laws traditionally had been limited to United States citizens and those who had declared their intent to become United States citizens.

In particular, debate in the Senate was principally directed at control of oil supplies, possible retaliation by foreign governments in response to a prohibition on foreign participation, the authority of the President and the Secretary of the Interior under the proposed amendment to section 1, and the possibility of trade embargoes. 48 Cong. Rec. 4112-4113, 4160-4171, 4281-4283 and 4785-4786 (1919).

The House debate focused upon whether to prohibit all foreign participation, the use of reciprocity both to retaliate against foreign governments which discriminate against United States interests and simultaneously to encourage foreign countries not to so discriminate, and a technical parliamentary question. 58 Cong. Rec. 7512-7515, 7527-7529 (1919). Unfortunately, the House did not debate the relative merits of reciprocity and the Senate provision authorizing takeovers. However, the House Report addressed the difference between the original Senate prohibition of foreign participation and the provision which was enacted. No. 398, at 11, supra. The reciprocity provision would, the House Report concluded, avoid foreign retaliations against U.S. interests and simultaneously address the Senate concern to prevent drain of U.S. mineral resources through export. The Report also noted that as a secondary and more drastic measure, Congress could prohibit exportation of domestic minerals through a general embargo if and when an acute situation arose.

In summary, the legislative history discloses the broad purposes of the reciprocity provision, but does not disclose the method by which the Secretary is to administer the provision. To the extent possible, the application of a statutory provision should be reasonably calculated to accomplish Congressional purposes. Accordingly, the reciprocity provision should, to the extent possible, be applied to prohibit the uncontrolled and unchecked exportation of domestic mineral resources and to discourage foreign retaliation against investment by United States interests.

B. Prior administrative interpretations

Since enactment of the Act of 1920, there has not been a dispositive administrative interpretation of the proper application of reciprocity. Nonetheless, several administrative options have been rendered addressing the operation of the reciprocity provision. The first interpretation came in 1920, when the Secretary of the Interior concluded that while a foreign country did not have to grant leases or permits to U.S. citizens and corporations to be reciprocal, the foreign country must allow United States citizens to organize corporations under the laws of the foreign country or to own, hold and control stock in that country's corporations. Letter, Secretary of the Interior to Secretary of State, dated October 19, 1920. (Attachment A.) In addition, the Secretary determined that stock participation by United States citizens must not, under foreign law, prevent the corporation from obtaining mineral development concessions or privileges on the foreign country's public lands. So long as stock participation by United States citizens was not precluded and so long as such participation by United States citizens did not preclude the corporation's mineral activities, the country would be considered reciprocal.

Then in 1936 the Solicitor concluded that Great Britain was a reciprocal nation even though companies were required to incorporate an operating company in Great Britain with at least one British director and a majority of British employees. Solicitor's Opinion M-28348 (April 2, 1936). (Attachment B.) In reaching this conclusion,

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the Solicitor relied upon a 1928 State Department conclusion that the Netherlands should be determined reciprocal because United States interests were authorized to participate in oil development in the Dutch East Indies, and the Dutch had actually permitted four oil development contracts to be executed. The Netherlands proscription against United States participation in oil development in Holland, as opposed to the Dutch East Indies, did not prohibit treatment of the Netherlands as a reciprocal country. Relying upon a similar analysis, the Solicitor reasoned that Great Britain was reciprocal. Furthermore, this Solicitor's Opinion was confirmed and ratified by the Attorney General who determined that the British incorporation requirements, even though the United States had no such provisions, were not "unduly restrictive or harsh." 38 Op. Att'y Gen. 476 (1936). (Attachment C.) The Attorney General also noted the British restrictions were akin to corporation laws of certain states and were therefore reasonable. Id. at 481. The Attorney General further concluded that a foreign country is not required to accord privileges to the United States interests identical to those accorded by the United States to aliens. Finally the Attorney General noted that the Secretary has a great deal of discretion in determining whether a country's "laws, customs or regulations" are "like or similar" to those of the United States.

In a memorandum approved by the Secretary of the Interior on November 18, 1939, the Commissioner of the General Land Office (predecessor to the Bureau of Land Management) discussed various aspects of reciprocity. (Attachment D.) First, the Commissioner stated that the provision "plainly contemplates" an "affirmative denial" of "like or similar" privileges for a country to be determined to be nonreciprocal. That is, as a procedural matter, the "laws, customs or regulations" must demonstrably prevent United States interests from enjoying the privileges granted to aliens by the United States. Second, the Commissioner acknowledged that the Department "has consistently followed the practice of inquiring into the laws, customs or regulations of that country with respect only to the particular mineral deposit as to which the foreign nationals desire to acquire an interest on the public lands" (emphasis added.) See Section IV below. Third, the Commissioner concluded that a foreign country may require some percentage of stock ownership by its citizens for a foreign corporation to qualify for mining concessions without affecting the country's status as a reciprocal nation. Finally, the Commissioner concluded that even though a foreign law dictated that the granting of mineral concessions is discretionary, the "laws, customs" and "regulations" should be construed as "like or similar" as long as it does not appear "affirmatively that the policy of the Government is to deny" mineral rights to U.S. citizens.

A more recent analysis of reciprocal, set out in a letter dated August 23, 1974, from the Deputy Solicitor to the Legal Advisor for Economic and Business Affairs, Department of State, was generated by the nationalization of the British coal industry. (Attachment E.) The Deputy Solicitor appropriately construed "like or similar privileges" to refer simply to the right of stock ownership, holding or control. After reviewing British laws, he determined that no British law prohibited United States citizens from owning stock in British corporations. The Deputy Solicitor therefore concluded that the bar to United States stock ownership in British corporations with coal interests arises not because United States citizens are denied the opportunity to own, hold or control stock in British corporations but only because British corporations cannot own coal interests. Since there was no discrimination between corporations based upon the ownership of stock, the Deputy Solicitor concluded that Britain did not deny "like or similar privileges" to United States citizens. Accordingly, Britain was determined to be reciprocal.

Finally, the Assistant Attorney General, Office of Legal Counsel, on August 11, 1981 concluded that the Secretary of the Interior has broad discretion to apply section 1 in a practical and flexible manner. (Attachment F.) In support of this concept, the Assistant Attorney General relied upon Section 32 of the Act (30 U.S. § 189) and found that pursuant to this discretion the Secretary may "mirror", to the extent possible, foreign restrictions on American investment in mineral development. Since the Assistant Attorney General was only addressing whether "mirroring" was permissible, he did not suggest that it is required.

C. Judicial Opinions

Since 1920, only two reported court decisions have involved the reciprocity provision and neither provides substantial guidance in determining whether a country is reciprocal. The first decision held that a private party had no standing to bring an action alleging that a foreign citizen owned an impermissible interest in a prospecting permit applicant. *Issacs* v. *DeHon*, 11 F.2d 943 (9th Cir. 1926). The second decision held that foreign stock holdings in the parent corporation of a lessee or appli-

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cant are only subject to the reciprocity provision if the stock holding is large enough to control the parent corporation. *No Oilport!* v. *Carter*, 520 F. Supp. 334, 359-60 (W.D. Wash. 1981), appeal pending.

Although there is a dearth of case law governing the implementation of the reciprocity provision, the courts have set forth certain well-established principles concerning the Secretary's authority to interpret and apply laws affecting mineral leasing. It is well-established that the Secretary possesses general powers of management over the public lands. *Boesche v. Udall*, 373 U.S. 472, 476-78 (1963); *Best* v. *Humboldt Placer Mining Co.*, 371 U.S. 334 (1963); *Orchard* v. *Alexander*, 157 U.S. 372 (1895); *Knight* v. *United States Land Association*, 142 U.S. 161 (1891). Moreover, the Mineral Lands Leasing Act generally was intended to expand, not limit, the Secretary's authority with respect to mineral lands. *Boesche* v. *Udall*, supra, at 481. The Secretary has the ability to establish reasonable interpretations and methods for accomplishing the purposes of the Act. *California Company* v. *Udall*, 296 F.2d 384 (D.C. Cir. 1961); *see also Thor Westcliffee* v. *Udall*, 314 F.2d 257 (D.C. Cir.); *cert. denied;* 373 U.S. 951 (1963); *United States* v. *General Petroleum Corp. of California*, 73 F. Supp. 225, 250 (S.D. Cal. 1946), *affirmed, Continental Oil Co.* v. *United States*, 184 F.2d 802 (9th Cir. 1950). Also, the Secretary has broad powers to administer mineral leases under the Act. *Udall* v. *Tallman*, 380 U.S. 1, 4 (1965). Accordingly, the case law specificially acknowledges the great discretion accorded the Secretary in applying the reciprocity provision of the Act.

III. THE DETERMINATION OF RECIPROCITY

The initial task in applying the reciprocity provision is to define the "privileges" granted to aliens in the United States which Congress sought to encourage foreign governments to provide, likewise, to citizens and corporations of the United States. Previous administrative interpretations have defined "privileges" as referring to the privilege of stock participation in United States corporations by foreign citizens. The basis of this interpretation, which was originally expressed in the 1920 letter of the Secretary of the Interior to the Secretary of State, has been scrutinized to determine if it is consistent with the statutory language and legislative history.

We have concluded for several reasons that this long-standing interpretation, which focuses first on stock participation, is a reasonable application of section 1 of the Act. Initially, the Act does not permit direct holding of mineral leases on public lands by foreign citizens or corporations. Rather, the Act grants foreign citizens an opportunity to participate in leases on public land, but only through stock ownership in domestic corporations. Since domestic corporations which meet the qualifications criteria may hold such leases, just as any other United States citizen, the key privilege granted by the United States is the right to stock participation. In short, through the vehicle of stock ownership, the United States permits foreign participation in mineral leases on public lands.

Therefore, the threshold issue which must be addressed in applying the reciprocity provision is whether U.S. citizens or corporations may own stock in the subject country's corporations. If after a review of the "laws, customs" and "regulations" of the foreign country you make a factual determination that there is an opportunity for U.S. citizens or corporations to own, hold or control stock in the foreign country's corporations, then that country should be presumed to be reciprocal. As a part of this analysis, if you make a factual finding that the "laws, customs or regulations" of the foreign country are "unduly restrictive or harsh," you should then determine if the foreign country provides other methods for investment in that country's minerals. 38 Op. Att. Gen., supra, at 481. "Unduly restrictive or harsh" means that the foreign country's "laws, customs or regulations" are so onerous, unreasonable, burdensome or so limit a corporation's privileges that the right of stock participation is rendered illusory or meaningless.

Finally, although a foreign country may permit meaningful stock participation in its corporations, that foreign country may, nonetheless, be nonreciprocal if it discriminates against United States interests by precluding or unreasonably restricting a corporation owned in whole or in part by United States interests from participating in the country's mineral resources on its public lands. For example, if such a corporation, because of the stock ownership by United States citizens, may not invest in the foreign country's minerals on public lands, the country should, in the absence of other investment opportunities, be determined to be nonreciprocal.

This procedure for determining reciprocity is compatible with existing procedures. For example, the Department has in recent years, in appropriate situations, applied a "mirroring" test to such stock limitations. This procedure was approved in the 1981 opinion of the Assistant Attorney General. Under the "mirroring" concept, if a

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country's "laws, customs or regulations" can be demonstrated to restrict ownership by a certain and definable percentage, such percentage ownership may be "mirrored" in applying the Act. However, as an administrative matter, it has been and will continue to be extremely difficult to ascertain with any degree of certainty the percentage of stock ownership permitted by a foreign country. Nonetheless, in instances where there is certainty as to the scope of a foreign country's restriction on stock participation by United States citizens, you may be able to make a reasoned and supported factual finding on the extent of such restriction. If you are able to make such a supportable factual finding, you may then "mirror" the percentage ownership permitted by the foreign country in your application of the reciprocity provision. If you find the "laws, customs or regulations" of other countries often cannot reasonably be interpreted with specificity, it is preferable to avoid speculation and conjecture and refrain from attempting to "mirror." Thus, the primary focus of a reciprocity inquiry should be whether the opportunity exists for United States citizens or corporations to own, hold or control stock in a foreign corporation. "Mirroring" may be applied where the Secretary has sufficient information to determine with precision the extent to which a foreign country is reciprocal.

The above analysis is appropriate in situations where the foreign country permits stock participation by United States citizens and corporations. However, in certain situations, the answer to the question of whether a foreign country permits stock ownership will not be dispositive of the reciprocity issue. Specifically, where a foreign country permits an opportunity for investment in its public mineral leases, it may be determined to be reciprocal. For example, if a country does not allow the formation of corporations but permits direct or other indirect participation on public land mineral leases, this may be sufficient to establish reciprocity. While this memorandum does not attempt to anticipate the wide variety of potential scenarios which may arise in the future, several elementary points should be noted. First, the Act grants lease rights only for certain enumerated minerals. These are the relevant minerals when determining a country's reciprocity. Second, the Act applies only to mineral leasing on public lands. Thus, in reviewing leasing privileges granted by foreign countries, we must look to foreign treatment of United States interests in connection with the foreign country's public lands.

If under the above analysis, you make a factual finding that a foreign country does not accord United States citizens and corporations the privilege of stock ownership in the corporations of that country, but it does accord the privilege of acquiring a beneficial interest in the minerals on its public lands, you may nonetheless find that the "laws, customs, or regulations" of the nation grant substantially equivalent investment opportunity in public mineral leases. In 1920, the Secretary of the Interior suggested that such a conclusion would be appropriate as long as the nation in question granted United States citizens and corporations "concessions":

"I suggest that you have our Minister advise the Netherlands Government that this Government does not contend that American citizens or American corporations should be granted leases or permits in the Netherlands as such, but that it does insist that Americans be permitted to organize corporations in and under the laws of the Netherlands, or to own, hold, and control stock in corporations organized by others under the laws of the Netherlands, and that such holding, ownership, or control shall not debar such corporations from obtaining *concessions or privileges* for the development of oil in the Netherlands or its colonies." (Emphasis added.)

Therefore, where the foreign country permits United States holdings of its minerals, even though not through stock participation, the country should nonetheless be determined to be reciprocal.

Finally, if a country imposes national treatment of its mineral industry or a portion thereof, and does not discriminate against United States holdings, the Deputy Solicitor's memorandum concluded that such treatment might not be a denial of "like or similar" privileges. (Attachment E.) While we have not reanalyzed that memorandum in detail, we have no reason to doubt its continuing validity. At your request, we will review that memorandum.

IV. DIFFERENT TREATMENT FOR DIFFERENT MINERALS

The question has arisen whether a country may be reciprocal for certain minerals and nonreciprocal for others. The legislative history discloses that Congress intended that there could be different reciprocity findings for different minerals. During the debate in the House of Representatives, Congressman Raker stated: "Guatemala does not permit an American citizen to own any of its sodium or phosphates. . . . Therefore a citizen of Guatemala cannot own any interest in *these* mines in this country." (Emphasis added.) 58 Cong. Rec. 7528 (October 25, 1919). In 1939 the Gen-

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eral Land Office adopted this position in a well-reasoned opinion. Since the statute is silent on this point, the Department has previously articulated this interpretation and the only related comment in the legislative history suggests a mineral-by-mineral approach, we find it reasonable to conclude that reciprocity may be determined on a mineral-by-mineral basis.

Such a finding may be made where the foreign country's "laws, customs or regulations" unreasonably discriminate against participation by a corporation held in whole or in part by United States interests in connection with some minerals, but not others. For example, if a country absolutely prohibits corporations with United States interests from holding any interests in oil but simultaneously allows corporations held by its citizens to hold such interests, the country would presumably be nonreciprocal for oil. (This assumes, of course, that the foreign country also prohibits other direct or indirect participation by U.S. interests in oil related activities.) However, if that same country does not so restrict investments in coal, it may be determined to be reciprocal for coal leasing. In short, a mineral-by-mineral approach is permissible where a foreign country's laws make such distinctions between minerals.

V. CONCLUSION

The Secretary has broad authority to develop a reasonable interpretation and implement appropriate procedures for applying the reciprocity provision. Reciprocity determination should focus initially on the opportunity of United States citizens or corporations to own, hold or control stock in foreign corporations. There must be no unreasonable and discriminatory prohibition on corporations with United States stockholders obtaining mineral rights, although nondiscriminatory prohibitions may be allowed. Finally, the inquiry may consider restrictions on stock ownership which apply to United States citizens but only to the extent they are "unduly restrictive or harsh." The Secretary also has the discretion to "mirror" foreign country's laws, where appropriate. In most cases, this presumably would involve a discriminatory denial of participation in mineral development. Opportunities for direct or other indirect participation as well as "nationalization" of a country's mineral industry should also be considerd in determining a country's reciprocal status. Finally, the reciprocity provisions may be applied on a mineral-by-mineral basis.

ALEXANDER H. GOOD,
Associate Solicitor, Energy and Resources.

SECRETARIAL DECISION PAPER: RECIPROCITY STATUS OF CANADA

In August 1981, the Department began a review of the general procedures for applying the so-called reciprocity provision of the Mineral Lands Leasing Act of 1920, 30 U.S.C. 81 (MLLA). At that time, the Department also began a review of the reciprocity status of Canada—a nation which has been listed as reciprocal for several years. The Solicitor's Office has prepared a memorandum, a copy of which is attached, establishing the basis for future decisions concerning the reciprocity status of nations. This paper applies this memorandum and presents a review of the laws and regulations in Canada which affect that nation's reciprocity status.

The analysis and recommedations of this paper should not be interpreted as a policy judgment on the part of the U.S. Government as to the appropriateness or inappropriateness of the laws, regulations, or customs of Canada. The MLLA requires a factual rather than a policy determination as to whether specific privileges accorded aliens in the U.S. are also accorded U.S. citizens and corporations in other nations. Indeed, that U.S. Government has serious reservations about the impact on U.S. citizens and corporations of the laws and regulations addressed in this paper. These reservations have been discussed with the Canadian Federal Government on several occasions and they continue to be discussed. Moreover, the U.S. Government is considering retaliatory measures directed against certain of the more onerous Canadian actions.

BACKGROUND

The review of Canada's reciprocity status was initated following petitions from the St. Joe Mineral Corporation and Conoco, Inc., each of which argued, in pertinent part, that the privileges accorded U.S. citizens in Canada under existing Canadian practices and proposed Canadian laws are not like or similar to the privileges accorded Canadian citizens in the United States under the provisions of the MLLA. In testimony before the House Subcommittee on Oversight and Investigations, you an-

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nounced your intention to review not only the question of Canada's reciprocity status but also to request public comments concerning this matter.

Public comments were requested by the Department in a *Federal Register* Notice published on November 12, 1981 (46 F.R. 55786). As of December 31, 1981, the date on which the Department closed this public comment period, a total of 34 comments had been received. These comments can be divided into two categories. The first category includes those comments which offer policy advice to the Department concerning either the question of Canada's reciprocity status or the question of actions the Department should take in response to Canadian laws, customs, and regulations. The second category includes those comments which offer analysis of the impact of Canadian laws, customs, and regulations on American citizens' privilege to obtain and hold interest in Canadian mineral resources. This paper incorporates only the contents of comments in the second category because the Department is required under the MLLA to make reciprocity decisions on the basis of a factual comparison of the privileges accorded American citizens under foreign laws with the privileges accorded citizens of other countries in acquiring interest in U.S. minerials leased under the MLLA. This paper also incoporates the representations made by St. Joe Mineral Corporation and Conoco, Inc., in their petitions to the Deparment.

SCOPE OF REVIEW

The Associate Solicitor has indicated that a mineral-by-mineral examination of reciprocity is acceptable. As such, this paper is concerned only with the Canadian laws that affect the privilege of American citizens to acquire interest in oil and gas deposits in Canada. This paper omits any discussion of American citizens' privileges concerning the acquistion of interest in other mineral resources because no evidence has been submitted to the Department to indicate that the privileges accorded to American citizens by Canada, with respect to other minerals, differ substantially from the privileges accorded Canadian citizens by the U.S. Therefore, should the Department decide that Canada is no longer reciprocal with respect to oil and gas, the privilege of Canadian citizens to acquire interest in minerals other than oil and gas leased under the MLLA will not be affected at this time. This policy of a mineral-by-mineral determination is not new; it merely affirms the Department's past practice.[1]

This paper also examines proposed Canadian laws which may affect Canada's reciprocity status in the future. The decision recommended in this paper is not drawn from proposed law, however. The Department believes that it is inappropriate, and the MLLA provides no mandate, to second-guess the actions of Canadain legislators who may consider legislation in the future that could be relevant to the reciprocity matter. The examination of proposed Canadian laws is provided here only for the purpose of illustration.

METHODOLOGY

This paper examines the reciprocity status of Canada in the following manner:

1. Each of the relevant Canadian laws, customs, and regulations are described and—omitted in original letter—citizens in the U.S.
2. Following the analysis of each Canadian law, custom, and regulation and explanation is given about the impact of the law, custom, or regulation on U.S. interests in Canada.
3. Alternative Departmental decisions concerning the reciprocity status of Canada are then presented along with a recommendation and supporting rationale.

THE RECIPROCITY TEST

The Associate Solicitor has determined that reciprocity decisions are usually to be made based on an initial two-part test. In the first part, the Department is to determine whether U.S. citizens are precluded by law, custom, or regulation from investing in the corporations of another nation through stock ownership, holding, or control. If the answer to this part of the test is that the nation does not preclude U.S. citizens in this respect, the nation is presumably reciprocal unless, in the second part of the test, the Department finds that U.S. investors are discriminated against by being effectively excluded from access to the mineral resources of the nation even though the nation may accord U.S. citizens the privilege of owning stock. Although this two-part test is likely to be sufficient for the purpose of examining the

[1] See, for example: Memorandum from the General Land Office to the Secretary, dated November 15, 1939.

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status of nations—including Canada—whose laws and regulations are straightforward, cases may arise in which the customs of a particular nation require further inquiry as the Associate Solicitor has noted in his memorandum.

This initial two-part test is based on the Associate Solicitor's interpretation that the similar or like privileges to which the MLLA refers is the right by stock ownership, holding, or control to own an interest in the mineral resources of other nations. This interpretation is also consistent with the legislative history of the Act and the Department's earlier interpretations of the statute,[2] as well as an opinion rendered by the Attorney General in 1936.[3] Moreover, it is consistent with recent Departmental decisions,[4] and was recommended by several of the organizations that responded to the Department's November 12, 1981, request for comments.

"The similar or like privileges" referred to in section 1 are the acquisition of stock interests. It was the intent of Congress that citizens of countries which deny United States citizens the right to acquire an interest by stock ownership, stock holding, or stock control in their domestic mineral extracting corporations not be allowed to acquire an interest by similar means in any lease issued pursuant to the Mineral Leasing Act of 1920. No intent to impose any further restriction on alien stock ownership was evident on the part of Congress." (Emphasis added)[5]

If the result of the two-part test outlined above and applied below is that American citizens are accorded the privilege of owning an interest in Canadian mineral deposits through stock ownership, holding, or control, then Canada should continue to be treated as a reciprocal nation within the meaning of the MLLA.

Some of the Canadian laws examined by Departmental staff in this review were found to be irrelevant under the test specified above. Nevertheless, they are discussed below to indicate why the Department has determined that they do not bear upon the issue of Canada's reciprocity status within the meaning of the MLLA. Despite the fact that these laws are extraneous to the factual determination the Department must make, they are of great concern to the U.S. Government and are the subject of actions that are being pursued through other, more appropriate forums (e.g., GATT Article XXII, OECD, and the Trade Act of 1974). As such, the fact that the Department does not consider these laws relevant to the issue of reciprocity should not be interpreted as endorsement of the conditions they impose on American citizens and corporations.

1. Foreign Investment Review Act, Stat. of Canada 1973, Chap. 46 (FIRA).

Requirements of the law.—This law establishes the Foreign Investment Review Agency (Agency) which is required to review certain acquisitions of existing Canadian corporatons and the creation of certain new Canadian corporations. The law requires that corporations attempting to acquire existing Canadian business or establish new Canadian businesses request approval of the Agency if (a) a total of 25 percent of the stock in such a corporation is owned by one or more aliens, (b) 40 percent or more of the stock is held in the corporation which is not publicly traded, or (c) 5 percent of the stock is owned by one individual who is an alien. The Agency is authorized to deny investment in Canada on the part of corporations required to report if the prospective investment is deemed by the Agency to be not "of significant benefit to Canada." The factors to be taken into account in determining what is of significant benefit to Canada are as follows: (a) the investment will increase the level of economic activity in Canada, including but not limited to increased employment; (b) the degree and significance of participation by Canadians in the new or existing corporation to be operated in Canada; (c) the effect of the acquisition or establishment on productivity, industrial efficiency, technological development, and product innovation in Canada; (d) the effect of the acquisition or establishment on competition in Canada; and (e) the compatability of the acquisition or establishment with national industrial and economic policies.

Analysis of the law.—FIRA contains no rule of general application that would prohibit American citizens or American corporations from acquiring interest by means of stock ownership, holding, or control in the oil and gas resources of Canada. FIRA is a general statutory prerequisite to any foreign corporation wishing

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[2] Memorandum of the Secretary of the Interior to the Secretary of State concerning the reciprocity status of the Netherlands, Oct. 19, 1920. See, also, Op. Cit., Memorandum from the General Land Office to the Secretary.

[3] 38 OP. Attorney General 476 (1936).

[4] For example, see Letter of David E. Lindgren, Deputy Solicitor of the Interior to Philip R. Trimble, Legal Advisor for Economic and Business Affairs—Department of State, dated Aug. 23, 1974.

[5] Memorandum of Sara Powell to the Assistant Solicitor, Branch of Onshore Minerals, concerning alien ownership and reciprocity, dated Aug. 10, 1978, p. 2.

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to do business in Canada. The factors that the Agency takes into consideration in reviewing prospective foreign investments suggest that FIRA is used by Canada as a means of insuring that commercial activities undertaken within their borders will be of economic benefit to the nation. These factors do not suggest that FIRA is intended to preclude, a priori, foreign investment in and control of Canadian oil and gas resources. One commenter (30) noted that the United States also monitors and, in certain instances, restricts foreign investment in various sectors of the U.S. economy but that such monitoring and restrictions are imposed by statutes other than the MLLA. Included among these restrictions are limitations on foreign ownership of nuclear energy and telecommunications facilities.

It, therefore, appears that the mere existence of laws such as FIRA does not compel a decision that Canada is a non-reciprocal nation within the meaning of the MLLA even though actions of the Agency may at times impede the free flow of capital across national boundaries. It appears that FIRA and regulations implemented by the Agency do not, a priori, deny American citizens or corporations the privilege of owning an interest in Canadian oil and gas resources through stock ownership, holding, or control.

Nevertheless, it is necessary to inquire as to whether it is the custom or practice of the Agency to deny American citizens or corporations this privilege. Some respondants to the Department's November 12, 1981, request for public comments noted difficulties they had encountered in acquiring approval from the Agency to make specific investments in Canadian oil and gas resources. Moreover, a review of the Agency's Annual Report indicates that in the most recent reporting year (1980–81) the Agency has, on occasion, refused to permit American corporations to acquire Canadian corporations which appear to have interest in Canadian oil and gas resources.[6]

The Annual Report also shows that most of the American corporations applying to the Agency with the intent of creating Canadian subsidiaries to explore for or develop Canadian oil and gas resources were approved. Although the Agency does not collect data specific to the oil and gas industry, their Annual Report shows that during the period 1980–81, 74.8 percent of all the applications for the acquisition of an existing Canadian corporation that would subsequently become controlled by a United States corporation were approved; 14.7 percent of such cases were disapproved; and 10.5 percent of the cases were withdrawn. Of the U.S. applications for new Canadian businesses in the year 1980–81, 78.7 percent were approved; 8.6 percent were disapproved; and 12.7 percent of the cases were withdrawn. These data show that it is neither the custom nor the practice of the Agency to deny U.S. citizens or corporations the privilege of acquiring an interest in Canadian oil and gas resources through stock ownership, holding, or control, a priori. To the contrary, the data show that the Agency has sanctioned the acquisition of oil and gas interest by Americans.

Therefore, Department staff believe that neither FIRA, its regulations, nor its administration provide a basis for altering Canada's existing status as a reciprocal nation within the meaning of the MLLA. It should be noted, however, that this conclusion could in the future change should the Agency alter its application of FIRA. Even though FIRA does not, in itself, deny U.S. citizens and corporations the privilege of investing in Canadian oil and gas resources, if the Agency were to institute such a ban in the future, it would be necessary to revise the conclusion stated above.

2. Canada Oil and Gas Production and Conservation Act, Stat. of Canada 1980–81, Chap. 81 (COGA)

Requirements of the law.—This law establishes separate licensing provisions for exploration and production activities only on so-called Canada lands, Canada lands include the Canadian Outer Continental Shelf, the Yukon, and Northwest Territories. This legislation does not affect oil and gas exploration or production activities on provincial lands.

A. In executing exploration agreements, this law (Section 9–16) does not differentiate between Canadian corporations which are wholly owned by Canadian citizens and Canadian corporations which are owned in part by citizens of nations other than Canada.

B. This law does differentiate between Canadian corporations which are totally owned by Canadian citizens and Canadian corporations which are only partially

[6] "Foreign Investment Review Act, Annual Report 1980–81," Government of Canada, Foreign Investment Review Agency.

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owned by Canadian citizens with respect to the granting of production licenses covered in Sections 17 through 25.

(1) Subject to Section 23, Section 19 requires that production licenses shall be granted or renewed only if: the individual seeking the license has been a resident of Canada for more than one year; or if a corporation is seeking the production license, it has a Canadian ownership rate of not less than 50 percent; or if two or more corporations seek the production license, their combined Canadian ownership rate equals 50 percent (see also Section 21), each one being determined by multiplying the Canadian ownership rate times its share in the interest.

(2) For the purpose of determining the Canadian ownership rate, the mandatory Crown share is considered as a 25 percent partner toward the 50 percent Canadian ownership minimum.

(3) If the corporation or joint venture seeking a production license does not have the mandatory 50 percent Canadian ownership rate, the Minister of Energy, Mines, and Resources is to notify the applicant of this deficiency. If the applicant fails to increase their Canadian ownership rate, the Minister is to assign an additional right to the Canadian Government equal to the difference between the Crown share and the existing Canadian ownership rate as determined above. Section 23 (1 and 2). The practical effect of this requirement is that production licenses will not be denied to Canadian corporations or joint ventures having a Canadian ownership rate of less than 50 percent. Instead, the provision would reserve to the Federal Government of Canada the right to increase the Crown share from the minimum of 25 percent.

(4) Sections 27 through 39 establish provisions for a 25 percent Crown share interest in all production licenses. When production licenses are held by more than one corporation, the Crown share is taken from a proportionate amount of each of the interests in the production license. For leases on which oil or gas was discovered on or before December 31, 1980, Section 29 provides that the license holders are entitled to a payment of 25 percent of their pre-1981 eligible investment for the purpose of compensating for the 25 percent Crown share. Payment is to be made only upon receipt of proceeds from oil and gas production.

(5) Section 40 provides that a basic royalty of 10 percent is to be paid on the oil and gas production from licenses.

(6) Section 41 provides that production license holders must pay a "progressive incremental royalty" payment equal to 40 percent of the net profit from oil and gas production. New profit for this purpose is determined after subtraction of the 10 percent basic royalty.

Analysis of the law.—The Associate Solicitor has determined that the Department should base its reciprocity decisions on the test of whether Americans have the privilege of acquiring stock in corporations of foreign nations and thereby acquire an interest in the mineral resources of that nation. Under this test, the requirement of COGA which mandates that corporations acquiring production licenses have a Canadian ownership rate of 50 percent or more does not deny American citizens or corporations the privileges accorded Canadian citizens under the MLLA. Nevertheless, it is clear that the Canadian ownership requirement is discriminatory toward United States citizens and corporations but it is so in a manner that does not affect the factual determination the Department must make concerning the reciprocity status of Canada within the meaning of the MLLA.

Some respondants to the Department's November 12, 1981, request for public comments stated the belief that the 50 percent Canadian ownership requirement on its surface compels the Department to find Canada to be a non-reciprocal nation within the meaning of the MLLA. While it is true that the requirement alters the opportunity for economic return from producing oil and gas on Canada lands, the requirement does not affect American citizens' and corporations' privilege of acquiring interest in Canadian oil and gas through stock ownership, holding, or control. As such, although the requirement may be of concern to U.S. corporations wishing to do business in Canada, it does not preclude such investment.

The Crown share requirement of COGA has an economic effect similar to the effect of a royalty. Although it clearly changes the revenue that corporations will receive as a result of oil and gas production, it does not deny American citizens or corporations the privilege of acquiring an interest in the oil and gas resources of Canada. Moreover, the Department notes that the Crown share is required of all corporations acquiring production licenses in Canada regardless of their Canadian ownership rate. Some of the respondents to the Department's November 12, 1981, request for comments expressed concern regarding the provision of COGA which would apply the Crown share retroactively. Departmental staff also note that the so-called "Crown share back-in" is the subject of international discussions between the United States and Canada. For the purposes of this analysis, however, the Crown

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share back-in provision does not alter the privilege of American citizens to acquire interest in Canadian oil and gas resources through stock ownership. As such, neither the Crown share provision or its back-in component indicate that the Department should modify Canada's current status as a reciprocal nation.

3. Energy Security Act, 1981: Petroleum Incentives Program Act, Schedule II (PIP)

Requirements of the Legislation.—The Energy Security Act and its component, PIP, were initially proposed by the Trudeau Government in October 1980. Legislation was introduced in the House of Commons in January 1982 and passage of the legislation is expected but not before April of 1982. Although this proposed legislation is not germane to the issue of Canada's reciprocity status within the meaning of the MLLA at this time because it has yet to be enacted, it will be discussed here in the context of the approach to determining reciprocity status set forth in the Associate Solicitor's memorandum.

The Energy Security Act would establish broad authority to regulate oil and gas production, distribution, and pricing. The PIP component of the Energy Security Act would be most pertinent to the issue of reciprocity should it be enacted. The PIP would establish:

A. The Petroleum Incentives Board which would be authorized to receive, from eligible Canadian corporations, applications for reimbursement of eligible exploration and development costs incurred in extracting oil and gas on Canada lands.

B. A sliding scale program of incentives through cost reimbursement based on the percent of Canadian ownership in the corporation exploring and developing Canada lands.

To be eligible for the minimum incentive payment, corporations would be required to have a Canadian ownership rate of at least 50 percent at the time exploration or development costs were incurred.

To be eligible for the maximum incentive payment, the corporation would be required to have a Canadian ownership rate of at least 75 percent.

C. It appears that the proposed legislation would use the approach specified in FIRA to determine Canadian ownership rates.

Analysis of the legislation.—All factors being equal, the proposed PIP would make the attractiveness of a given oil and gas venture on Canada lands more attractive to a corporation that was 100 percent Canadian owned than to a corporation that was only 50 percent Canadian owned.

Despite the fact that the proposed PIP would affect the attractiveness of investments on Canada lands based on the corporation's Canadian ownership rate, the legislation does not compel the Department to conclude that Canada is a non-reciprocal nation within the meaning of the MLLA. The proposed incentives are the economic equivalent of an investment tax credit. The incentive program, as it is currently written, does not deny American citizens or corporations the privilege of investing in oil and gas resources on Canada lands through stock ownership, holding, or control. Thus, the proposed legislation does not constitute a basis for altering Canada's existing status as a reciprocal nation.

4. Other Canadian laws

Canada currently regulates the wellhead price of crude oil to approximately 65 percent of the world market price. The Canadian Federal Government has expressed its intent, through the proposed National Energy Program and, in particular, through the proposed Energy Security Act, to maintain crude oil price controls for the immediate future. Price controls vary according to the age of the oil field, the depth of the discovery, and the nature of the product extracted. Canada proposes to decrease the level of control during the period 1982 through 1986 by allowing the crude oil price to rise to approximately 85 percent of the world market price.

Although the U.S. Government has expressed its concern over Canada's existing and proposed oil price control structure on the grounds that it does not promote efficient development of oil and gas resources, oil price controls are not germane to the issue of Canada's reciprocity status within the meaning of the MLLA. This is true because:

1. Price controls do not discriminate against foreign ownership or control of the corporation extracting the oil or gas resource.

2. Price controls do not deny American citizens or corporations the privilege of investing in Canadian oil or gas resources through stock ownership, holding, or control, even though such controls clearly affect the economic attractiveness of Canadian investments, all other factors being equal.

The COGA (Section 10 (No. 3)) establishes the explicit goal of encouraging oil and gas companies operating in Canada to make use of equipment and materials suppli-

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ers that are Canadian. It accomplishes this by providing that Canadian energy companies are to make use of Canadian suppliers rather than suppliers from other nations when the prices offered by Canadian suppliers are "competitive." As in the case of oil price controls, the purchasing objective of COGA is the subject of concern to the U.S. Government but it is not relevant to the Department's review of the reciprocity status of Canada. This is true for the reasons stated in the paragraph above.

THE RECIPROCITY DECISION

Decision

You are faced with three basic options in making your factual determination concerning the reciprocity status of Canada.

Option 1: Fully Reciprocal.—Acceptance of this option would essentially reaffirm Canada's existing status as a reciprocal nation within the meaning of the MLLA. This option would impose no restrictions on Canadian citizens or corporations wishing to acquire an interest in U.S. mineral leases issued under the MLLA. If you find that the laws, customs, and regulations of Canada currently do not deny U.S. citizens the privilege of stock ownership, holding, or control—the test established in the Associate solicitor's memorandum and outlined in the preceeding pages, you should choose this option.

Option 2: Reciprocal to a Specified Percent ("Mirroring").—Acceptance of this option would allow Canadian citizens or corporations to own up to a specified percent of the stock in U.S. corporations seeking to acquire mineral leases under the MLLA in the future. If you find that the COGA in practice, although not in law, effectively prohibits American citizens or corporations from acquiring more than a specified percent ownership of Canadian corporations extracting oil and gas from Canada lands, you should choose this option.

Option 3: Non-Reciprocal.— Acceptance of this option would preclude Canadians from acquiring an appreciable percentage of the stock of any U.S. corporation seeking to acquire leases issued under the MLLA. If you find that the mere existence of FIRA and COGA effectively deny United States citizens and corporations the privilege of acquiring interest in Canadian oil and gas through stock ownership, holding, or control even though these laws do not explicitly prohibit such a privilege, you should choose this option. Moreover, in accepting this option, you must find that there are no other investment vehicles available to U.S. citizens and corporations to acquire an interest in Canadian mineral resources and that Canada precludes only aliens from investing in its resources.

RECOMMENDATIONS AND CONCLUSIONS

Based on the preceeding analysis, it is recommended you find Canada to be reciprocal within the meaning of the MLLA.

It is not recommended that you find that Canada is non-reciprocal (Option 3) because the Department's review indicates that Canadian laws, customs, and regulations do not deny U.S. citizens or corporations the privilege of acquiring an interest in the mineral resources of Canada. Moreover, it is not recommended that you find that Canada is reciprocal to a specified percent (Option 2) even though you could attempt to "mirror" the provisions of Canadian law, COGA in particular. It would, however, be extremely difficult to "mirror" COGA with the precision advised by the Associate solicitor in his memorandum. This is true because COGA does not deny production licenses for Canada lands based on foreign ownership, regardless of the percentage of such ownership. Instead, COGA requires a larger Crown share for corporations, the stock of which is totally or principally owned by non-Canadians, than is required of corporations the stock of which is owned only be Canadian citizens. As such, if the Department were to limit Canadian ownership of U.S. corporations holding mineral leases, the Department would have established a restriction that is substantially different from, and more onerous than, COGA.

If the finding recommended in this paper is adopted, it is important to separate the decision that Canada is a reciprocal nation within the meaning of the MLLA from the on-going activities of the U.S. Government in expressing serious concern over the impact of existing and proposed Canadian policies. As stated earlier in this paper and in the Associate solicitor's memorandum, the MLLA reciprocity test is indeed narrow in its scope. It is a factual, two-part test of whether specific nations accord American citizens the privilege of investing in oil and gas resources through stock in a manner that is similar to the privileges we accord citizens of those nations. On the other hand, the concern that is now being expressed by the U.S. Government concerning Canada's overall economic and energy policies is based upon

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the tenets of international investment and trade as expressed in GATT, the OECD, and in U.S. legislation such as the Trade Act of 1974. Under these tenets the U.S. Government is now seeking to promote a policy of open investment in which capital is free to flow among nations to its most efficient use, and to protect existing American interests in Canada and in other nations. The Department of the Interior is fully in accord with this policy and is working with other Executive Branch departments and agencies to promote it.

APPENDIX B

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS OF THE COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C., June 24, 1981.

The PRESIDENT,
The White House
Washington, D.C.

DEAR MR. PRESIDENT: The House Energy and Commerce Committee is concerned with the increasing problems U.S. investors seem to be having as a result of discriminatory treatment by the Canadian Foreign Investment Review Agency (FIRA). The FIRA has refused to allow investment in certain fields in Canada by non-Canadians, and has even blocked the transfer between U.S. corporations of Canadian assets. This adverse treatment is certain to become even more pronounced once the National Energy Program (NEP) is passed by the Canadian Parliament. The effect of these actions has been and will increasingly be to depress the earnings prospects for American-owned companies in Canada. Taken with the actions of the FIRA, which effectively restricts the marketability of U.S. subsidiaries in Canada to Canadian buyers, these policies devalue the Canadian assets of U.S. corporations and thereby injure their millions of stockholders.

The NEP has several purported objectives, such as security of supply and development of energy resources, which may be admirable but it also contains various disincentives for U.S. investors including:

The establishment of an objective of at least 50 percent Canadian ownership of the petroleum industry by 1990:

A system of incentives for oil exploration and development which is biased in favor of companies with a high degree of Canadian ownership while reducing the competitive viability of foreign-owned Canadian companies;

The requirement that a company must have at least 50 percent Canadian ownership before obtaining a production license on "Canadian lands";

A guaranteed 25 percent back-in interest for the government-owned oil company, Petro-Canada, on all successful oil and gas exploration on "Canadian lands"; and

New taxes on oil and gas for financing Canada's takeover of presently foreign-owned companies.

Considering such developments, the Oversight Subcommittee convened a hearing on June 19 at which representatives from Conoco, Cities Service, St. Joe Minerals, and Lehman Brothers testified. The first three companies have been directly and adversely affected by Canada's actions. Conoco recently exchanged its 52.9 percent interest in Hudson's Bay Oil and Gas of Canada for Dome Petroleum of Calgary's recently acquired 22 million Conoco shares plus $245 million. It was economically coerced into doing so under difficult and unfair circumstances caused by Canada's economic nationalism and the lack of adequate response to these policies by our government. Cities Service is fighting an effort by Nu-West Group Limited (Nu-West), a Canadian corporation, which has purchased 6 million shares (more than 7 percent) of Cities Service stock, to exchange for valuable Canadian oil and gas properties at distressed prices. St. Joe Minerals was forced to sell CANDEL Oil Ltd. in which it had a 92 percent share, to raise cash in order to resist a takeover attempt by Seagrams Ltd., a Canadian Company.

The testimony before the Committee documents the following serious problems resulting from Canadian policies:

The NEP discriminates against foreign-owned companies in contravention of Canada's international commitments;

Canada's Foreign Investment Review Agency provides the Canadian government an effective tool to control and exclude foreign investment as it sees fit;

The effects of the National Energy Program and Foreign Investment Review Agency reinforce each other. The NEP depresses the value of assets held by American companies in Canada, as well as the future earnings potential of a foreign-controlled company while FIRA blocks any non-Canadian competitive bidding for the

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stock. This permits Canadian companies to then acquire the American assets at "fire-sale" prices;

American interests in energy companies were sold under duress at depressed prices to Canadian firms which paid for such by trading U.S. stock in an affiliated company purchased under financial conditions not available to any other American company;

The financial advantage accruing to Canadian firms comes from the existing practice in the United States of the Federal Reserve margin requirement. U.S. companies can use only 50 percent of the price of tendered shares as collateral for loans while Canadian firms can receive 100 percent loans from their banks; and

The Mineral Lands Leasing Act of 1920 allows foreign participation in mineral leases on federal lands only if a foreign country allows reciprocal privileges to U.S. citizens. Clearly, the NEP, as presently proposed, as well as the activities of FIRA, are direct violations of the reciprocity requirement.

A legislative solution may be required to counterbalance these unfair policies of the Trudeau Government. Since this should be avoided if possible, it would appear that the first course of action would be a clear and strong U.S. diplomatic initiative to convince Canada to voluntarily change its policies. The Ottawa Economic Summit on July 20 and 21 provides an ideal opportunity for you to express the U.S.'s serious concerns over Canada's expanding discriminatory investment, energy, and trade policies to Prime Minister Trudeau while the Secretaries of State and Treasury and the U.S. Trade Representatives should reinforce this argument with their counterparts. We would point out that the OECD has already publicly disapproved of the thrust of the Canadian policies. In these discussions, it should also be pointed out to Prime Minister Trudeau that developing countries are watching closely Canada's policies which, if enacted, would undermine the efforts of other industrialized countries to encourage adoption by these countries of fair and equitable standards for international trade and investments.

Our Committee plans to have subsequent hearings prior to the Summit meeting on this subject and will be shortly extending invitations to Secretaries Haig and Regan and possibly other Administration personnel.

We again strongly urge you to make this matter a high priority at the Summit meeting because of the adverse effect the Canadian policies have on the interests of U.S. citizens.

Sincerely,

JOHN D. DINGELL,
Chairman,

JAMES T. BROYHILL,
Ranking Minority Member.

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APPENDIX C

DEPUTY U.S. TRADE REPRESENTATIVE,
EXECUTIVE OFFICE OF THE PRESIDENT,
Washington, D.C., August 26, 1981.

Hon. JOHN D. DINGELL,
Chairman, Subcommittee on Oversight and Investigations, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Thank you for your letter of August 13, 1981, asking for my recommendations for action in response to Canada's National Energy Program (NEP) and Foreign Investment Review Agency (FIRA).

The President, in his July 10 meeting with Prime Minister Trudeau, noted our concerns with both the NEP and FIRA. I do not believe the issue was brought up at the Ottawa Summit.

An interesting development which can be related to the activities of FIRA and the proposed NEP is the decline of the Canadian dollar. All along, we have been stressing to the Canadians that their policies will have an adverse economic effect on the Canadian citizens. We now see the Canadian dollar at a 50-year low, inflation heating up, and a slowing of the investment flow to Canada. This will result in less jobs for Canadians.

As I mentioned to you in our response to your July 13 letter to the President, the investment and Canada subcommittees of the interagency Trade Policy Staff Committee (TPSC) met jointly to initiate a review, to culminate in mid-September, which will (1) consider in detail the impact of U.S. interests in FIRA and the NEP; (2) develop U.S. objectives which focus on Canada's investment and energy policies; and (3) outline U.S. options and recommend actions designed to realize our objectives. The purpose of this review is to develop a response in a systematic and comprehensive manner rather than an ad hoc basis. The TPSC's main objective is to develop appropriate options which will be effective in modifying the Canadian position while avoiding damage to our own interests.

This review is now underway and although we do not expect it to be ready for TPC review before September 9, we would like to cooperate with you in whatever way we can. I think we share a common perception of the problems caused by Canada's policies and the need to devise the best way to approach a solution to this issue.

Sincerely,

DAVID R. MACDONALD.

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APPENDIX D

THE U.S. TRADE REPRESENTATIVE,
Washington, D.C., August 21, 1981.

Hon. JOHN D. DINGELL,
Chairman, Committee on Energy and Commerce, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Thank you for your letter of July 16, 1981 to the president concerning the adverse impact of U.S. interests of recent Canadian Government actions. The Administration is very sensitive to the potentially serious impact on U.S. interests of the Canadian Government's current investment policies as manifested in the National Energy Program (NEP) and the Foreign Investment Review Agency (FIRA).

Our concerns in this regard have been raised repeatedly at the highest levels of the Canadian Government. In ongoing diplomatic exchanges we have made clear our position that the Canadian Government should, in accordance with its international obligations, adhere to the "national treatment" principle embodied in the General Agreement on Tariffs and Trade (GATT). In addition, the President has expressed his concerns to Canadian Prime Minister Trudeau over the impact of Canada's investment policies on our bilateral relations. To date, as you are undoubtedly aware, our diplomatic efforts to modify the objectional aspects of the NEP and FIRA have achieved only marginal success.

Accordingly, on August 13, the investment and Canada subcommittees of the interagency Trade Policy Staff Committee (TPSC) met jointly to initiate a review, to culminate in mid-September, which will: (1) consider in detail the impact on U.S. interests of FIRA and the NEP; (2) develop U.S. objectives which focus on Canada's investment and energy policies; and (3) outline U.S. options and recommend actions designed to realize our objectives. The purpose of this review is to develop a response in a systematic and comprehensive manner rather than on an ad hoc basis. The TPSC's main objective is to develop appropriate options which will be effective in modifying the Canadian position while avoiding damage to our own interests.

We expect to stay in close coordination with you throughout this process.

Sincerely,

DAVID R. MACDONALD, *Acting.*

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APPENDIX E

THE SECRETARY OF COMMERCE,
Washington, D.C., August 31, 1981.

Hon. JOHN D. DINGELL,
Chairman, Subcommittee on Oversight and Investigations, Committee on Engery and Commerce, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with your request, enclosed is a description of our investment problems with Canada, our views on Canadian obligations to the United States in the area of investment, and some remedies that may be useful in helping to resolve these issues. Thank you for the opportunity to provide my assessment of the situation.

Sincerely,

MALCOLM BALDRIGE,
Secretary of Commerce.

Enclosure.

U.S.-CANADIAN INVESTMENT RELATIONS

U.S. INVESTMENT POLICY

The traditional policy of the U.S. Government toward international investment—neither to promote nor discourage inward or outward investment flows or activities—is consistent with our longstanding commitments to an open international economic system. It is based on the belief that international investment will generally result in the most efficient allocation of economic resources if it is allowed to flow according to market forces. With reference to foreign equity investments in the United States, our policy is to permit them freely and unconditionally on a non-discriminatory basis, and to grant them equal treatment with domestic investors. A few exceptions exist in certain sectors of the economy which have a fiduciary character or relate to national security, nuclear energy, and the exploitation of federally-owned land.

At the same time we respect the right of each country to determine in accordance with its own priorities the environment in which foreign investment takes place in that country. However, once investments have been made on that basis, we believe governments should not discriminate against them on the basis of nationality. The United States has an important interest in seeking to assure that established investors receive equitable and non-discriminatory treatment from host governments.

The global deterioration of economic conditions in recent years, coupled with limited financial resources and rising energy costs, have resulted in many developed and developing countries offering incentives or levying preformance requirements on foreign investment to achieve specific economic objectives. These objectives include attracting investment, increasing exports, decreasing imports, and channeling investment to poorer regions of the country.

Canada's investment policies—which have become increasingly restrictive since the mid-1970's—have been especially troublesome to us. Our trading and investing relationship with Canada is so extensive that the negative effects of Canada's policy changes fall mainly on the United States and have a significant effect on our investment, trade, and balance of payments. Furthermore, because Canada is a major industrialized nation, what it does in the international economic sphere is likely to give encouragement to others to do the same.

FOREIGN INVESTMENT REVIEW AGENCY

In the early 1970's Canada established the Foreign Investment Review Agency (FIRA) to screen two types of foreign direct investment: new investments by both

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new and old investors into new fields, and acquisitions. Investment proposals are evaluated for eight factors: (1) job creation; (2) the number of Canadians in management on the board of the acquired company; (3) improvement of existing facilities and/or expansion; (4) increased research and development in Canada; (5) local purchasing; (6) expanded exports; (7) Canadian partnership or ownership; and, (8) reinvestment of earnings. Approval is granted when there is "significant benefit" to Canada.

This policy presents a number of serious problems:

U.S. company agreements with Canada on import reduction and export expansion are of special concern as they reduce U.S. exports to Canada, decrease U.S. exports to third country markets, and increase U.S. imports.

Such agreements are legally binding and, although Canada has clarified its policy to apply only when Canadian goods are "competitively available," we believe these agreements are in voilation of GATT (General Agreement on Tariffs and Trade) Article III.

FIRA review of a company's expansion into an unrelated area of business (e.g., a paint company's purchase of a furniture manufacturer) inhibits a company from diversifying and improving its profitability.

FIRA review of mergers betweens U.S. parent companies that involve transfer of ownership of a Canadian subisidiary (whether or not the merger results in an increased level of foreign ownership of the Canadian subsidiary) has extraterritorial applicability and has the capacity to necessitate a forced sale of a Canadian subsidiary by the acquiring U.S. company. This has expropriatory implications and can reduce U.S. exports to Canada since 75 percent of the imports from the United States of the 300 largest firms in Canada represent intracompany transactions between a U.S. parent and a Canadian branch or subsidiary.

FIRA is disallowing expansions by foreign-owned gas and oil companies into non-energy sectors of the Canadian economy, again limiting growth potential via diversification.

While FIRA's approval rate is fairly high (even though it has fallen in the last year from 90 percent to 75 percent) such statistics do not reflect the hard bargaining that transpires between the Canadian Government and U.S. companies or those applications never made due to anticipated rejection.

Furthermore, we understand it is the Canadian Government's intention to institute a number of new proposals in the fall which will exacerbate the situation.

The performance of major established foreign companies would be reviewed for "significant benefits" to Canada.

Takeovers by foreign companies would be reviewed at public hearings.

Such takeovers would be held in abeyance for 30 days to allow bidding by domestic companies.

The Secretary of Commerce and other high level Commerce officials have discussed these issues on several occasions with high level officials in the Canadian Ministry of Industry, Trade, and Commerce (ITC), including ITC Minister Gray. The Canadians, however, have not indicated that they would take account of our concerns except on minor points. As result of U.S.-Canadian discussions in Ottawa on May 27—at which Commerce was represented by Joseph F. Dennin, Deputy Assistant Secretary of Finance, Investment and Services—FIRA will likely reduce the secrecy involved in U.S. company-FIRA negotiations and, under certain circumstances, allow a representative of the U.S. Government to be present at those negotiations.

In an attempt to quantify FIRA's trade damage to the United States we have formulated a questionnaire—which has just been cleared through OMB—to go to the Industry Sector Advisory Committees (ISAC's), the Fortune 500, and both approved and disapproved U.S. applicants to FIRA asking about their commitments to Canada and the FIRA process. With this information we could judge the probability of success of going into the GATT on the basis of impairment of tariff concessions and Canadian discrimination against imported products.

Because Canada listed FIRA as an exception to the national treatment provisions of the 1976 Organization for Economic Cooperation and Development (OECD) agreement on international investment and multinational enterprises, we have not called for consultations on FIRA in the OECD. However, if Canada extends FIRA's operations to include a review of the performance of established companies, this would constitute a massive, new derogation from the agreement and we would call for consultations. While the OECD has no formal sanctions, the views and esteem of other member countries are valued and could cause a country to modify its policies.

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THE NATIONAL ENERGY PROGRAM

On October 28, 1980, as part of its budget message, the Canadian Government announced a far-reaching National Energy Program (NEP), designed to ensure 50 percent (up from 30 percent) Canadian ownership of the oil and gas industry in Canada by 1990 and full Canadian control of "several" large, foreign-owned oil and gas companies. The U.S. Government has critized the NEP virtually since its announcement. Our criticisms have centered on the following:

The 25 percent "back in" provisions require a 25-percent share of oil and gas production revenues to go to the Canadian Government on a retroactive basis, essentially without compensation.

The intent to maintain a "Canadian Oil Price" at 85 percent of the world (or Chicago) price could be viewed as a subsidy to exports.

The lower price discourages Canadian self-sufficiency in oil.

Under the Petroleum Incentives Program, earned depletion allowances will be phased out and replaced by a subsidies program with the amount of the subsidy proportional to the level of Canadian ownership in an oil and gas company.

Only those firms or consortia which are at least 50 percent Canadian owned will be permitted to participate in the extraction of oil and gas from "Canada Lands."

The two items listed immediately above may not only negatively affect U.S. investors' earnings and assets but they are also a major derogation from the OECD principle of national treatment.

As a result of numerous U.S. Government written and oral exchanges with Canada and consultations in March within the OECD in which Commerce participated, Canada recently modified the NEP. On May 14 Energy Minister Lalonde announced that Canada will modify the industrial-benefits provisions in the bill to stipulate that Canadian suppliers of goods and services should have a "fair but competitive" opportunity to share in procurement related to oil and gas exploration and development activities on Canada lands without discriminating against non-Canadian suppliers. This provision would be similar to the one in FIRA and admittedly, leaves a great deal of room for interpretation as to what is "competitive".

We also were pleased to hear that Canada would pay a portion of the exploration costs incurred by companies on Canadian lands, although first indications are that the amount to be offered may be inadequate. This is a welcome alteration in the so called "back-in" provisions of the NEP, although, the basic impact of the NEP is still detrimental to the United States.

We have a number of options for dealing with the NEP. First, we will continue consultations with the Canadians in the OECD. Six other OECD nations have joined us in voicing serious concerns about the discriminatory aspects of the NEP and its departure from the OECD agreement on national treatment.

Second, the Administration has asked the Interior Department to accelerate its investigation of the reciprocity provisions of the Mineral Lands Leasing Act of 1920. Under this law, Canadian firms may be denied access to leases on U.S. federally-owned lands for certain minerals on the grounds that Canadian laws, customs or regulations deny like access to corporate or private citizens of the United States. The Administration is also analyzing the usefulness or extending reciprocity provisions such as those found in the Mineral Lands Leasing Act to off-shore areas as well. Third, if we find that the trade aspects of the NEP remain inconsistent with Canada's obligations, we will pursue the issue through the GATT mechanism.

CANADIAN INVESTMENT IN THE UNITED STATES

The introduction of the Canadian National Energy Program has sparked a number of Canadian investments in U.S. oil and gas companies, particularly those with investments in Canada. In these cases, a Canadian Company buys up large amounts of a U.S. company's shares, and then offers the shares and control back to the U.S. company in exchange for the U.S. company's Canadian property. For example, Conoco recently agreed to trade its 52.9% interest in Hudson's Bay Oil and Gas Co. for Canada's Dome Petroleum Ltd.'s $1.68 billion in cash and stock. In other cases, when a U.S. company with a Canadian subsidiary merges with, or is acquired by, a non-Canadian company, the transaction must be reviewed by FIRA and often results in divestiture of the Canadian subsidiary.

On June 30, the Committee on Foreign Investment in the United States (CFIUS)—for which Commerce provides staff assistance—concluded that several of these Canadian attempts to take over U.S. companies resulted from the NEP in that U.S. energy and minerals firms often needed to sell off their Canadian assets, resulting in bargain prices. CFIUS referred these issues for review to the Trade Policy Committee because of their trade policy implications. CFIUS will still monitor and

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review cases for their adverse implications for U.S. policy implementation, an coordinate the executive agencies that have responsibility for implementing federal laws and regulations affecting foreign investment activity in the United States. In addition, CFIUS has agreed to review all Canadian acquisitions in the United States related to the NEP.

We believe, as you do, that some of this takeover activity has been furthered by foreign companies having access to bank loans in their home countries that are not subject to the U.S. 50 percent margin requirement. However, we also believe that requiring foreign investors to abide by U.S. margin requirements would be difficult to enforce since creative financing from a variety of sources is fairly easy to arrange. In addition, the flow of capital into the United States from sources other than Canada could be restricted to the detriment of both the United States and the foreign source.

THE AUTOMOTIVE AGREEMENT

As a result of taking control of American Motors Corporation (AMC), Renault has had to apply to FIRA for approval of its takeover of AMC's Canadian subsidiary. If AMC/Renault were to increase Canadian value added as a condition for FIRA approval, the Administration would report it to Congress in accordance with Section 205(b) of the Automotive Products Trade Act of 1965. This Act provides that "whenever the President finds that any manufacturer has entered into any undertaking, by reason of governmental action, to increase the Canadian value-added of automobiles, buses, specified commercial vehicles, or original equipment parts produced by such manufacturer in Canada after August 31, 1968, he shall report such finding to the Senate and the House of Representatives. The President shall also report whether such undertaking is additional to undertakings agreed to in letters of undertaking submitted by such manufacturer before the date of enactment of this Act."

The issue is complicated by the fact that last year AMC failed to satisfy its production-to-sales ratio requirement, a Canadian safeguard associated with the Automotive Agreement. This failure was due in part to lower Canadian production caused by a retooling at AMC's Brampton, Ontario plant and higher Canadian sales due to the inclusion of Renault imports in AMC's sales figures. (Renault can now take advantage of AMC's ability to import motor vehicles duty free under the Auto Pact.) Discussions with AMC indicate that they hope to work out an arrangement to cover the shortfall by future production. An increase in Canadian production by AMC/Renault to meet production-to-sales requirements might also help AMC/Renault's case before FIRA by showing the Canadian Government that the Renault takeover did provide benefits for Canada.

BANKING

Although the Canadian Bank Act of 1980 constitutes a significant liberalization of the climate for foreign banks, major restrictions still exist. Foreign banks can now establish full-service subsidiaries in Canada, but their Canadian assets cannot exceed 8% of the total domestic assets of the Canadian banking system. However, the 8 percent ceiling does not apply to loans made to Canadian residents from offices in the United States. Furthermore, during the President's visit to Ottawa, Finance Minister MacEachen assured Secretary Regan that the Act will not be implemented in a discriminatory manner.

The U.S. policy of national treatment of banks has brought new technology, wider range of financial services, and an increased capital supply. We believe Canada will continue its liberalization steps as the benefits of an open financial market become visible.

CONCLUSION

We have, as yet, no evidence that unilateral U.S. Government intervention in the international investment process would further the U.S. national interest. The United States is the single largest overseas investor and we have been a world leader in the promotion of a free trading and investing system. A U.S. policy that would restricit inflows of foreign capital would more likely have an adverse effect on the U.S. economy by slowing the flow of capital, technology, and managerial expertise to the United States. If also could lend support to other countries' arguments for their own restrictive policies. Because of the seriousness of our investment problems with Canada and the possibility of certain retaliatory acts damaging the U.S. economy, we are engaged in a policy review both within the Department of Com-

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merce and through appropriate interagency groups to assess our options and to make a determination as to how we can be successful in our efforts to protect U.S. interests.

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DISSENTING VIEWS

Without in any way sanctioning, approving or acquiescing in the discriminatory and protectionist trade and investment practices fostered by the Canadian Government of Prime Minister Pierre Trudeau, we respectfully dissent from certain of the characterizations, conclusions, and recommendations of the Subcommittee Report.

We dissent not without some reluctance. We do not wish to give any comfort to the Canadian governmental officials who have instituted these damaging policies, nor give any signal to the Administration that we, as Members of Congress, endorse any policy of "turning the other cheek" or ignoring the ramifications of Canada's myopic policies. However, the Subcommittee Report makes unfair characterizations, draws incorrect inferences, and suggests certain remedies that we cannot permit to go unchallenged.

CANADA'S TROUBLED DOMESTIC ECONOMY

According to the U.S. Trade Representative, at the end of 1981 U.S. investment in Canada had surpassed $46 billion, compared with $12 billion of Canadian investment in this country. Two-way trade between the countries amounts to better than $80 billion annually. This economic interdependence makes Canada's current, restrictive policies even more short-sighted, for there can be no doubt that each nation has economically benefited from the free flow of capital and trade across the other's border.

Underlying Canada's policies is a desire to reduce the large U.S. capital investment in that country, particularly in the oil and gas sector. When the National Energy Program [NEP] was adopted in 1980, foreign interests, mostly American, controlled more than 70 percent of Canada's oil and gas industry. The goal was to make Canada self-sufficient in energy and to reduce foreign control of the energy sector to 50 percent by 1990.

As correctly pointed out in the Subcommittee Report, the effect of the "Canadianization" policy has been to discourage or deter further U.S. investment in Canada's energy sector and to limit, and thus devalue, the market for the sale of Canadian assets of U.S. corporations.

The unintended effect of Canada's policies has been a flight of capital from the country. Ironically, this capital flight ($18 billion in the last 2 years) has come not only from foreign investors, but Canadian investors themselves concerned about the re-sale market for their domestic investments. Canada finds itself in the midst of its worst economic crisis since the Great Depression. Unemployment stands above 11 percent of the workforce and inflation is still mired at the 12 percent level. Business bankruptcies have multiplied, and corporate profits have plummeted by nearly 50 percent

during the first six months of 1982 over year-earlier periods. The Canadian dollar is trading at the $.80 mark in relation to the U.S. dollar, its lowest value in 50 years.

We take no comfort in Canada's domestic difficulties, noting that our own unemployment rate is too high and that U.S. business bankruptcies and corporate profits are heading in the wrong directions. We do recognize, however, that the strength of the U.S. dollar stems from several factors, including a declining rate of inflation and favorable political, tax and investment climates.

As long as Canada's restrictive and discriminatory policies remain in force, the flow of capital will continue to run southward. Prompted, however, by a rising internal chorus of opposition, headed by the provincial governments, the banks and the business community and the opposition political party, and premised upon Canada's rapidly deteriorating domestic economy, it appears that Trudeau is backing off from the nationalistic "Canada First" policies that have no doubt contributed significantly to the economic problems faced by Canada in 1982.

With its rising budget deficits, high unemployment and declining domestic productivity, Canada's investment and trade policies are simply the wrong dose of economic medicine at the wrong time.

We believe that the likely effect of Canada's misguided policies, enacted as far-sighted visions of an independent Canada, but in reality a noose around her status as an interdependent member of the free world, was apparent to the Secretary of the Interior and to those who counseled him regarding the decision whether to find Canada to be "non-reciprocal" within the meaning of the Mineral Lands Leasing Act of 1920 (30 U.S.C. Sec. 181 et seq.).

Accordingly, we believe it is understandable that our government would not seek to "rachet up" the stakes of a potential trade and investment war with our long-time economic partner by finding Canada to be "non-reciprocal," particularly when Canada's domestic economic scenario may cause a voluntary roll-back of dismantling of the objectionable features of both the NEP and FIRA.

Potential Adverse Effects of Non-Reciprocity Finding

The Subcommittee Report fails to discuss how a finding of non-reciprocal status as applied to Canada would be beneficial to U.S. interests. Such a finding would, of necessity, deny to Canadian investors the privilege and right of investing in U.S. companies with Federal mineral leases. It would also have required the cancellation of existing leases on Federal lands for those U.S. companies unable to successfully force the sale by Canadian investors of their stock holdings.

Such a finding is likely to have had several unintended and adverse effects:

(1) U.S. corporations and U.S. energy projects would be denied an important source of equity capital;

(2) Since Canada is seeking to maximize domestic ownership of its oil, gas and mineral sectors and discourage the flow of limited capital beyond its borders, finding Canada to be non-reciprocal would play directly into her hands;

(3) By cancelling mineral leases of U.S. companies with Canadian stockholders, the U.S. Government would have been unwittingly devaluing the assets of U.S. companies;

(4) Such an action would be at odds with the objective of the U.S. Government to foster free trade and investment policies among the nations participating in the General Agreement on Tariffs and Trade [GATT] and Organization for Economic Cooperation and Development [OECD].

Administration Efforts

Although the Subcommittee Report alleges that the Administration was dragging its feet on the reciprocity question and not making efforts to modify the Canadian policies, the evidence is clear that various agencies of the U.S. Government were involved in assessing the problem and evaluating the tools available to protect U.S. economic interests.

On October 21, 1981, Raymond J. Waldmann, Assistant Secretary for International Economic Policy of the Department of Commerce, testified before the Subcommittees on International Economic Policy and Trade and on Inter-American Affairs of the House Committee on Foreign Affairs. Waldmann outlined an eight-point program of initiatives being pursued by the Administration in light of Canada's protectionist policies. These efforts were as follows:

(1) Consultations on the NEP are continuing with the Canadians, in the OECD. Other OECD nations have joined us in voicing serious concerns about the discriminatory aspects of the NEP and its departure from the OECD agreement on national treatment;

(2) In an effort to determine the specific extent to which FIRA's performance requirements affect the flow of economic resources, we are conducting a survey of U.S. firms' investment activities in Canada. The survey was sent to approximately 1,000 firms representing members of the U.S. Government's Private Sector Advisory Committees, the Fortune 500 and firms known to have made investment proposals to FIRA.

(3) The Administration has asked the Interior Department to accelerate its investigation of the reciprocity provisions of the Mineral Lands Leasing Act of 1920. The Administration is also analyzing the usefulness of extending reciprocity provisions such as those found in the Mineral Lands Leasing Act to off-shore areas as well;

(4) If we find that the trade aspects of the NEP or FIRA are inconsistent with Canada's GATT obligations, we will raise this issue in the GATT;

(5) On the issue of the CIRB [Committee on Industrial and Regional Benefits (Canada)], Canada informs us that this committee will conduct reviews of energy-related projects on Canada lands and self-initiated reviews on other projects. We still need to consult with the Canadians on this issue;

(6) CFIUS [Committee on Foreign Investment in the U.S. (U.S.)] will continue to monitor and review inward investments for any adverse implications for the United States, and coordinate the executive agencies that have responsibility for implementing Federal laws and regulations affecting foreign investment activity in the United States;

(7) In an attempt to improve our dialogue with the Canadians, last week Secretary Regan held useful discussions with high Canadian officials in Ottawa. The principal subjects discussed were FIRA, the NEP, and the CIRB; and

(8) Most importantly, we are engaged in interagency review of U.S. investment policy, both inward and outward as well as a review of U.S. trade and investment policy toward Canada, specifically.

We also believe that the testimony of Mr. Waldmann on October 21, 1981, which follows may be further instructive of the myriad issues at play in the reciprocity determination, and why it was incumbent that Secretary Watt not make this decision either hastily or precipitously.

While we should take action with regard to unfair treat ment of U.S. investors abroad, we should be surfe that any reaction should not be significantly detrimental to our own interests. The ultimate results should not adversely affect the United States. We need to be cautious about modifying outward investment policies and bilateral investment agreements because of the potential damage to individual U.S. businesses here and abroad who have succeeded in earning a profit, exporting, or securing raw materials while accommodating other countries' restrictive policies.

We also need to be cauticus about limiting foreign investment in the United States because of the benefits we receive from it. A stable and secure investment climate is one of the major strengths of our economy and a major source of our prosperity. Actions which raise doubts among potential foreign investors as to our continued support for an open and free international trade and investment commitment woujld be harmful to our domestic interests. In this regard, we must take into account that the United States is a major force in international trade and is the largest single investor overseas. Furthermore, the United States has been a major force in liberalizing trade and capital flows throughout the world.

Effort to Impugn the Motives of Secretary Watt Is Misdirected

We believe that the decision-making process outlined by the Secretary of Interior in his appearance before the Subcommittee on August 6, 1981, in which the Secretary articulated the steps he would follow in reaching a decision on whether Canada was a "reciprocal country" within the meaning of the Mineral Lands Leasing Act, was reasonable and perhaps even necessary. These steps were explained by Secretary Watt as follows:

To respond to your questions and to comply with the Department's mandate under the Mineral Lands Leasing Act, I have initiated a formal fact-finding effort to determine whether Canada should be declared nonreciprocal and, if so, what actions should be taken by the Department.

The purposes of this effort are to protect the rights of all interested parties to due process under the law and to arrive at a decision that is in the best interests of the U.S.

The fact-finding effort will involve the following steps: First, I will make a formal request that the heads of all relevant Federal agencies give me their opinions on what standards should be applied in making reciprocity decisions, whether Canada is a reciprocal nation under these standards, and, if Canada is not a reciprocal nation, what steps should I take in applying the Mineral Lands Leasing Act.

Second, I will review these recommendations and decide whether there is sufficient evidence that Canada is not reciprocal to proceed with our review.

If such evidence exists, I will publish a notice in the Federal Register requesting public comments. Upon the closing of the public comment period, I will make a preliminary determination as to Canada's reciprocal status.

Finally, after a review of all relevant evidence, I will decide whether Canada is a reciprocal nation, and, if it is not reciprocal, what sanctions should be applied.

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The Secretary's decision on this matter was announced on February 2, 1982, a period of slightly less than six months after his appearance before the Subcommittee and his enumeration of the steps to be followed in reaching the decision. We do not believe that this is an unreasonable amount of time, particularly when, as acknowledged in the Subcommittee Report, little more than ad hoc procedures previously existed within the Department of Interior for reviews of this type, given the level of economic interests involved in the canadian determination, and given the interests of other agencies of the government.

Conclusion

The protectionist and discriminatory policies of the Canadian government are a burden on the free flow of investment capital between Canada and the U.S., and have the effect of devaluing Canadian assets of U.S. corporations. The Administration must use all means at its disposal to protect and defend U.S. trade and economic interests. In an increasingly interdependent world, the U.S. must demonstrate that free and fair trade is a two-way street. While we believe that a finding that Canada was non-reciprocal may have been more harmful to our own interests than to Canada's, we believe that efforts should be intensified to gain modifications in Canada's restrictive policies. The current state of Canada's domestic economy provides an opportunity where those efforts might be more likely to achieve results consistent with U.S. interests.

James T. Broyhill.
N. F. Lent.
Harold Rogers.
Dan Coats.
Bob Whittaker.
Don Ritter.

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